TAC ÑONG CUA HIEP ÑÒNH THÖÔNG MAI
SONG PHÖÔNG VIET NAM - HOA KY
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THE IMPACT OF THE U.S.-VIETNAM BILATERAL TRADE AGREEMENT ON OVERALL AND U.S. FOREIGN DIRECT INVESTMENT IN VIETNAM

NHA XUAT BAN CHÍNH TRÒ QUOC GIA
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Bao cao nay khong nhat thiet the hien quan ñiem cua Cô quan Ho trô phat trien quoc te Hoa Ky, Chính phu Hoa Ky hay Bo Ke hoach va Ñau tö cua Viet Nam, Chính phu Viet Nam.

THE IMPACT OF THE U.S.-VIETNAM BILATERAL TRADE AGREEMENT

ON

OVERALL AND U.S. FOREIGN DIRECT INVESTMENT IN VIETNAM

PREFACE AND ACKNOWLEDGEMENTS

The Foreign Investment Agency (FIA) of the Ministry of Planning and Investment (MPI) and the U.S. Agency for International Development (USAID)-funded STAR-Vietnam Project have been requested by the Vietnamese Government Steering Committee for Technical Assistance on BTA implementation and the U.S. Agency for International Development (USAID) to provide analysis on the impact of the U.S.–Vietnam Bilateral Trade Agreement (BTA) on overall and U.S. foreign direct investment in Vietnam.

This Report is prepared by an MPI Research Team consisting of: Ms. Nguyen Thu Huong, Team Leader and Manager, Policy and Statistics Department, FIA; Ms. Le Hai Van and Mr. Nguyen Viet Cuong, Senior Experts, Policy and Statistics Department, FIA; and, Dr. Nguyen Ngoc Anh, Consultant, Lecturer of Economics, Hanoi Business School. The Research Team was directed by Mr. Phan Huu Thang, General Director of the FIA. A preliminary draft of the Report was reviewed thoroughly at a technical workshop on May 5, 2005 that was organized by the FIA.

USAID provided funding and technical support for the development of this Report. In this regard, the report benefited from comments by STAR-Vietnam experts, including: Mr. Steve Parker, Project Director; Mr. Phan Vinh Quang, Deputy Project Director; and Ms. Do Hoang Anh, Training and Policy Specialist. Substantive comments and contributions were also provided by Mr. Nguyen Anh Tuan and Ms. Mai Thi Thu, Vice Directors of the FIA; Mr. Nguyen Xuan Trinh, Vice President, Central Institute for Economic Management; Mr. Tran Hao Hung, Vice Director, Legal Department of the MPI; and, Dr. Vu Quoc Huy, Economist at the Institute for Economics and Development, Vietnam Academy of Social Sciences. This report also benefited from the guidance and support provided by Mr. Dennis Zvinakis, Vietnam Country Manager of USAID.

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STAR-Vietnam is an economic growth project funded by the U.S. Agency for International Development (USAID) to assist Vietnam to implement the U.S. – Vietnam Bilateral Trade Agreement and to accede to the World Trade Organization.

EXECUTIVE SUMMARY

With the coming into effect of the U.S.-Vietnam Bilateral Trade Agreement (BTA) on December 10, 2001, Vietnam and the United States normalized trade and investment relations. On the day the BTA came into effect, the U.S. extended normal-trade-relations (NTR), which is more commonly known as most-favored-nations (MFN), treatment to Vietnam. This action lowered the average tariff on imports from Vietnam to the U.S. from around 40 percent to around 4 percent. This effectively opened the huge U.S. market to Vietnamese exporters on an equal footing with other foreign competitors. As well, the BTA required that Vietnam phase in, over a ten-year period, changes in many laws, policies, regulations, and administrative procedures that are, in large part, based on WTO standards and international best practice.[1] The comprehensive set of obligations in the BTA for both countries was expected to stimulate not only bilateral trade between the two countries, but also to increase the attractiveness of Vietnam for U.S. and many other foreign investors.

This Report is prepared by the Foreign Investment Agency (FIA) of the Ministry of Planning and Investment (MPI) in cooperation with experts from the USAID-funded STAR-Vietnam Project. It represents the first attempt to analyze in detail the response of foreign direct investment (FDI) to the BTA.[2] In particular, the Report presents comprehensive data on U.S. FDI sourced directly from the United States, which we call "reported U.S." or "U.S.-based" FDI, and

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1. The BTA has comprehensive requirements covering trade in goods and services, intellectual property right protection, the development of investment, commercial dispute settlement, business facilitation, and transparency and the right to appeal. For a more detailed description of the BTA, its link to the WTO, and the subsequent bilateral trade response to the coming into effect of the BTA, see the 2002 Annual Report on "An Assessment of the Economic Impact of the U.S.-Vietnam Bilateral Trade Agreement," and the "Update on Bilateral Trade in 2003 Between Vietnam and the United States," both produced by the Central Institute of Economic Management (CIEM) and STAR.

2. This Report examines FDI only. It does not include other forms of foreign investment, such as portfolio investment in capital markets, and does not assess what should be the important impact of the BTA on domestic investment. In this regard, FDI would include such investment by overseas Vietnamese under the Foreign Investment Law but would exclude investment made by overseas Vietnamese that may be registered as domestic investment under the Domestic Investment Encouragement Law.

FDI from overseas subsidiaries of U.S. firms, the combination of which we call "U.S.-related" FDI. In interviews conducted for this study, U.S. firms in Vietnam noted that U.S. tax laws and business considerations related to the still relatively small size of the Vietnamese domestic market encourage U.S. firms to invest in Vietnam from regional headquarters, most commonly Singapore and Hong Kong, as well as to some degree from other third countries with more favorable tax reporting requirements. As well, since the BTA's Chapter IV on the "Development of Investment Relations" covers investment by U.S. overseas subsidiaries just as strongly as it covers FDI funded directly from a home office in the United States, FDI from U.S. overseas subsidiaries should be expected to respond to the BTA. In the current statistical measure of FDI (which counts only FDI sourced directly from one country to another), this FDI from U.S. subsidiaries resident in third countries is reported as FDI from that resident country (e.g. from Singapore, not the United States).[3] It seems clear, however, that the full response of U.S. firms to the BTA should be assessed in terms both of FDI funded directly from the U.S. and FDI funded by U.S. overseas subsidiaries. In fact, the results in this Report show that U.S. firms responded more aggressively in expanding FDI to Vietnam from their overseas subsidiaries than from home offices in the United States.

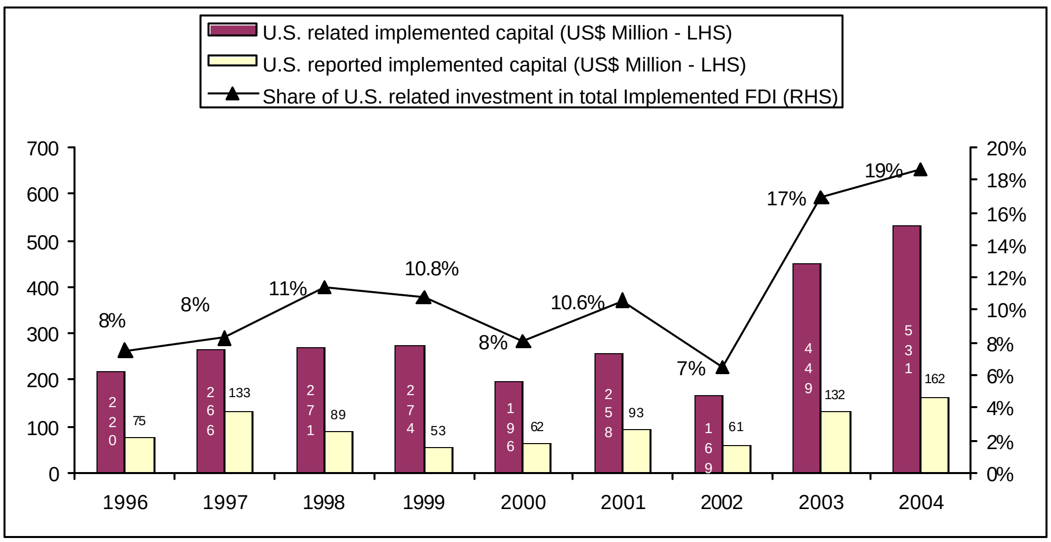
The reported U.S.-based FDI data commonly presented by MPI show that U.S. FDI has increased relatively moderately since the BTA came into effect in 2001. This fact has led many to note that although bilateral trade has boomed since the BTA came into effect, U.S. FDI has not responded significantly to the BTA reforms. The new MPI data on U.S.-related FDI developed for this Report, however, reveal a different story. First, accumulated U.S.-related FDI implemented from 1988 through 2004 is US$2.6 billion compared to the reported FDI amount of US$730 million (see Table 7 in the text). This shows that FDI into Vietnam by U.S. firms has been considerably higher than was commonly reported for many years. Secondly, U.S.-related FDI has increased strongly since the coming into effect of the BTA, growing by an average of 27 percent a year from 2002 through 2004 compared to just around 3 percent a year from 1996 to 2001 (see Figure 1 and Table 8 in the text). In 2004, U.S.-related FDI of US$531 million was the largest type of FDI into Vietnam, above FDI sourced from Japan, Korea, Singapore and Taiwan, the countries most typically considered to be the largest investors into Vietnam (see Table 9 in the main text). This quantitative

3. As is typical for most reporting on FDI throughout the world, reported FDI in Vietnam designates the origin of FDI as the country where the funding of the investment originates. This importantly and accurately measures capital flows from one country to another, but, as noted, it does not adequately capture how many U.S. multinational companies manage their investment decisions.

data shows that FDI from U.S. firms have responded strongly since the BTA came into effect. Though in absolute terms, the growth of U.S.-related investment in Vietnam remains modest as compared to the boom in the bilateral trade, the share of U.S.-related investment in total overall implemented FDI in 2004 is around 20 percent, almost the same percentage as Vietnamese exports to the U.S. to overall Vietnamese exports.

Figure 1: Implemented U.S. FDI into Vietnam

(US$ millions)



Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

The strong response of U.S.-related FDI to the BTA is confirmed by the results of a survey of 81 foreign firms conducted for this Report (32 U.S-related, 47 non-U.S. and 2 unidentified). The survey shows that 49 percent of participating enterprises considered the BTA in their decision to make or expand their investment in Vietnam. This figure is 53 percent for U.S. companies and 43 percent for non-U.S. companies. In general, companies that exported to the U.S. registered higher growth in investment, export sales and employment after the BTA than those that did not export to the U.S. or those that did not consider the BTA in their investment.[4]

Key commitments in the BTA highlighted by foreign firms, and especially U.S. firms, as being most important to improve the investment climate in Vietnam include improving transparency, removing discrimination between foreign and local firms, using a registration system for investment licensing, improving IPR

4. In this report, "BTA investors" are investors who responded that they considered the BTA in making/expanding their investment in Vietnam, while "non-BTA investors" did not.

protection and opening more sectors for foreign investment. U.S. firms also considered effective commercial dispute settlement procedures to be important. When all considerations for improving the business and investment environment are taken into account, not just those emphasized by the BTA, foreign-invested firms stressed the importance of enforcing laws evenly and effectively, of joining the WTO and of improving the tax and investment licensing systems. U.S. firms compared to non-U.S. foreign firms stressed the importance of tax, trade and investment agreements. Although firms responding to the survey noted that the investment environment in Vietnam had clearly improved recently, importantly in part as a result of the BTA, they clearly stress the importance of continuing to develop a more transparent legal system with more effective, uniform and predictable enforcement of laws and policies.

Despite the significant increase of U.S.-related investment, the room for further development is great. Total U.S.-related FDI in Vietnam is less than 1 percent of the total U.S. investment in the region, and equal only to 28 percent of U.S. FDI in Thailand and 20 percent of U.S. FDI in Indonesia in 2003.[5]

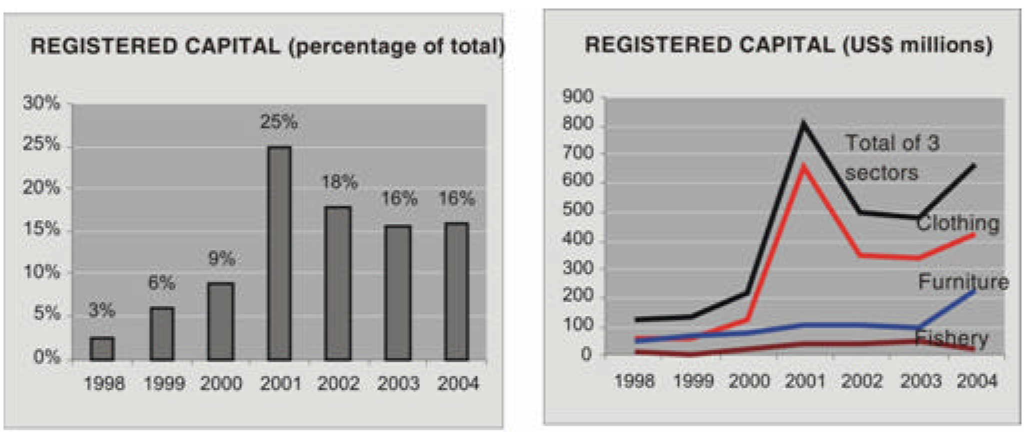
The Report also examines the impact of the BTA on overall FDI, which includes FDI from all countries including the United States. Why would we expect that overall FDI would increase in response to the BTA, since the BTA is a bilateral not a multilateral agreement? First, the BTA was viewed by many Vietnamese and foreigners alike as a path-breaking and irreversible commitment by Vietnam's leadership to develop a market-based economy that would integrate strongly into the world economy. Second, even though the BTA was a bilateral agreement that included obligations only directly for Vietnam and the U.S., both countries promoted that the BTA was a key "stepping stone" toward acceding to the WTO, where a broad range of commitments would be applied on a most-favored-nations (MFN) basis to all WTO members trading and investing with Vietnam. Vietnam's solid progress over the last several years toward meeting the requirements to accede to the WTO reinforces all the more this perspective. Third, many of the reforms required for BTA implementation were done by Vietnam on an MFN basis, so that all foreign and domestic parties benefited. And, fourth, the BTA-related provision of NTR/MFN treatment to Vietnam served to open up overnight the huge, receptive U.S. market for Vietnamese exports, which greatly increased incentives for many countries other

5. By 2003, total U.S.-related implemented FDI in Vietnam was US$2.1 billion whereas U.S. (reported) FDI in Thailand and Indonesia was US$7.4 billion and US$10.4 billion, respectively (source: Ministry of Planning and Investment of Vietnam and U.S. Department of Commerce).

than the U.S. (especially East Asian neighbors) to invest in Vietnam to produce typically labor-intensive exports for the U.S. market.

After a spike in the mid-1990s, overall FDI into Vietnam has grown quite modestly (see Figure 3 in the text). When compared to general, large declines in FDI worldwide from 2000 to 2003, however, Vietnam's moderate growth in FDI over this period actually looks relatively robust (see Table 1 in the main text). There is little indication from the aggregate FDI data into Vietnam, nevertheless, that the BTA has had an important impact on foreign investment into Vietnam. A closer look at the sectors widely perceived as having the greatest potential for exports to the U.S. market, however, reveals a stronger response to the BTA.[6] Figure 2 shows that after the BTA was signed in 2000, overall FDI in clothing, furniture and fishery grew substantially.[7] The share of these sectors in total registered FDI rose from 3 percent in 1998 to 25 percent in 2001, and then stabilized at 16 percent in 2003 and 2004.

Figure 2: Registered FDI in Clothing, Furniture and Fisheries



Source: MPI.

In summary, from our analysis of newly developed quantitative data and firm survey results, we can conclude that the signing and implementation of the BTA have played an important role in promoting FDI into Vietnam, particularly for U.S.-related FDI, and for improving the business environment in Vietnam. This conclusion, however, should be qualified. This Report, which is based on an

6. MPI experts and company interviews for this Report reveal that FDI in these sectors since 2000 was aimed primarily to build capacity to export to the U.S. as a result of the BTA-related opening of the U.S. market for Vietnam-based exporters.

7. The BTA was signed by the two governments on July 13, 2000. It was passed by the U.S. Congress on October, 3, 2001 and signed by the U.S. President on October 16, 2001. It was ratified by Vietnam's National Assembly on November 28, 2001 and signed by the President of Vietnam on December 7, 2001. The BTA came into force on December 10, 2001.

analysis of descriptive data, represents only a first step toward understanding how the BTA, and soon the WTO, affects FDI into Vietnam. No attempt is made in this Report, for example, to develop a sophisticated economic model that can isolate the impact of the BTA by controlling for other factors that affect investors' decisions. We encourage in particular more research on the impact of the BTA on domestic investment, which we expect to have been positive and significant, but which we have not been able to analyze in this Report. To facilitate further research, the Research Team would be happy to provide more details on the data and survey results presented in this Report.

I. OBJECTIVES, SCOPE AND METHODOLOGY

The U.S.-Vietnam Bilateral Trade Agreement (BTA), which normalized trade and investment relations between the two countries when it came into effect on December 10, 2001, marks an important step in Vietnam's course of economic integration. After three years of entry into force, bilateral trade between the two countries increased from US$1.4 billion in 2001 to over US$6 billion in 2004, of which exports from Vietnam to the U.S. increased from US$1 billion in 2001 to US$5 billion in 2004, while U.S. exports to Vietnam doubled over this period.[8] Such spectacular trade growth was beyond the expectation of many people. The impact of the BTA on foreign and U.S. direct investment, however, appears to have been less visible and in many ways has not met the expectations of many. It is important for policy makers and business leaders to understand how overall foreign FDI and, in particular, U.S. FDI into Vietnam have responded to the BTA. With the approval of the Steering Committee on Technical Assistance Program for Vietnam-U.S. BTA implementation and USAID, the Foreign Investment Agency (FIA) has cooperated with STAR-Vietnam to conduct a study to assess the impact of the BTA on U.S. and overall FDI into Vietnam.

As the first report examining this issue in Vietnam, the Research Team undertook to shed light on several basic questions. First, how has overall FDI been affected by the BTA? Second, how has U.S. FDI responded to the BTA-related reforms? Lastly, we examine how Vietnam can attract more FDI into Vietnam after three and half years of BTA implementation and in the context of the pending WTO accession agreement. Given the limited data available in Vietnam, the Research Team and MPI developed several new sources of information. First, based on reports and updates from almost all provinces, the MPI reviewed as many foreign-invested projects that have been approved and implemented as possible to determine whether a project was conducted by a U.S. overseas subsidiary, in addition to the FDI sourced directly from the United States. With this data, MPI developed a new metric to evaluate U.S.-related FDI, which adds FDI from U.S.

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8. See the CIEM/STAR 2002 Annual Report on *An Assessment of the Economic Impact of the U.S.-Vietnam Bilateral Trade Agreement,* and the *Update on Bilateral Trade in 2003 Between Vietnam and the United States* for a more detailed description of the bilateral trade response to the coming into effect of the BTA.

subsidiaries resident in third countries to FDI sourced directly from the United States and which we call "U.S.-related" FDI. U.S.-related FDI represents how much U.S. multinational companies have invested in Vietnam, not how much FDI has come directly from the United States.[9] To calculate this new FDI data, MPI determined how much U.S.-overseas-subsidiary FDI came from which resident country. At this time, it was not possible to make this same calculation for FDI from other countries, which means that we cannot re-rank on a consistent basis U.S.-related FDI relative to other countries' related FDI.

In addition to this new quantitative data, the Research Team also conducted a survey of 81 foreign-invested firms, including 32 U.S. firms, 47 non-U.S. foreign firms, and 2 foreign firms without a national identification. As well, seven in-depth interviews were conducted with U.S. and foreign firms operating in both the South and North of Vietnam.

This Report aims to provide an initial examination of how FDI has changed since the coming into force of the BTA, with a focus on newly developed descriptive data on U.S.-related FDI. A more sophisticated economic model is not developed, so that it is not possible to determine carefully what influence the BTA had on FDI flows relative to the many other factors affecting decisions to invest in Vietnam. The firm survey was conducted to explore how firms say they responded to the BTA. We see this Report as a first step, but by no means the last step, in examining how the BTA (and soon the WTO) affects FDI to Vietnam. To facilitate further research, the Research Team would be happy to provide more details on the data and survey results presented in this Report.

This Report consists of eight parts. Part II reviews the investment commitments contained in the BTA and examines how successful implementation of these commitments could affect FDI to Vietnam. Part III analyzes how overall FDI into Vietnam has responded since the BTA has come into effect. Part IV examines how U.S. FDI to Vietnam has responded to the BTA, with a focus on U.S.-related FDI flows. Part V explores Vietnam's nascent FDI outflows and how it has responded to the BTA. Part VI assesses the results of a mail-out survey of U.S. and non-U.S. foreign firms with regard to the importance of the BTA to their investment decisions and company performance. Part VII summarizes foreign firms' opinions on the link between implementation of the BTA and how to improve Vietnam's business environment to attract more FDI. A conclusion and suggestions for further research are included in Part VIII.

9. Note that reported FDI from the U.S. consists of all FDI sourced from the U.S., including non-U.S. multinationals based in the United States. Based on available MPI data, however, there does not appear to be any non-U.S.-firm FDI sourced from the U.S. into Vietnam.

II. THE U.S.-VIETNAM BILATERAL TRADE AGREEMENT AND IT'S EFFECTS ON THE ENVIRONMENT FOR FDI TO VIETNAM

A. Investment Commitments under the U.S.-Vietnam Bilateral Agreement

The BTA is the most comprehensive trade agreement ever entered into by Vietnam. Investment is a key part of the BTA. The scope of investment covered by the BTA is not limited to direct investment. It also includes indirect investment, including equity, bonds and other tangible and intangible assets. As an agreement modeled on the WTO framework, the BTA includes all WTO commitments on investment, including:

- Eliminating trade-related-investment measures (TRIMs);
- Opening up service markets for foreign investment under a schedule;[10]
- Non-discrimination and elimination of dual price systems; and
- Transparency in the promulgation and implementation of investment policies.

As well, the BTA contains other provisions that go beyond the WTO Agreements and that are similar to those in typical investment protection agreements, such as the Vietnam-Japan Agreement on the Protection and Encouragement of Investment concluded two years after the BTA. Important commitments in the BTA that are not covered in the WTO include:

- Eliminating export performance requirements (which are not covered by TRIMs);
- Allowing licensing by registration for many U.S.-invested projects, except for those in specified sensitive sectors;
- Removal of restrictions on equity contribution, the consensus principle for corporate governance in joint ventures, and some other limitations on the establishment and management of U.S.-invested enterprises;

10. The WTO accession agreement will most likely require a greater number of service sectors to be opened than did the BTA commitments, with shorter if any phase in schedules.

- Allowing U.S. investors to set up joint stock companies and to issue securities in Vietnam; and
- Provision of improved investment protection procedures and dispute settlement mechanisms between U.S. investors and the State, including access to international arbitration under ICSID.[11]

Some of the investment commitments in the BTA mentioned above were required to be applied over the first three years of BTA implementation, while a number of others were to be phased in over subsequent years. Timely and consistent implementation of these commitments will help improve the investment climate in Vietnam.

B. A Review of How BTA Investment Commitments Have Been Implemented

In recognition of the importance of the BTA to international integration and improving the business environment in Vietnam, the National Assembly of Vietnam issued Resolution No. 48/2001/QH10 dated November 28, 2001 instructing various government agencies to amend laws and regulations to implement the BTA. Vietnam has implemented some important commitments in the BTA, and is scheduled to revise thoroughly by the end of 2005 its overall legal framework for investment and enterprise registration by developing a new Common Investment Law (CIL) and a new Uniform Enterprise Law (UEL). The CIL and UEL are expected to harmonize foreign and domestic investment and enterprise registration regimes and are expected to liberalize access by foreign investors to a number of sectors, particularly service sectors. The exact market access reforms will be determined by the final resolution of the WTO accession negotiations, and will be applied on an MFN basis to all WTO members. Below is a brief review of the progress that has been made on implementing investment commitments in the BTA.[12]

- ***National Treatment (NT) and Most Favored Nation (MFN):*** The Ordinance on MFN and NT provides a general legal framework for extending NT and MFN to foreign investors and traders. The CIL and UEL are expected to deal specifically with all key NT issues related to investment.

11. ICSID: International Center for Settlement of Investment Disputes. This is an arbitration center for resolving investor-state disputes established as part of the World Bank Group.

12. This review does not necessarily represent the view of the U.S. or Vietnamese Governments. It represents the understanding and professional assessment of the Research Team.

- ***Removal of Dual Pricing*: ** As of January 1, 2005, with adjustments for electricity, Vietnam completed its obligation to remove all dual pricing for services provided to foreign businesses.[13]
- ***Removal of the Limitation on Technology Transfer*: ** Decree 27/2003/NÑ-CP removed the requirement that foreign contribution in the form of technology must be less than 20 percent of equity.
- ***Mortgage of Land Use Rights*: ** The Foreign Investment Law and new Land Law allow foreign investors to mortgage land use rights at credit institutions licensed to operate in Vietnam.
- ***Eliminating TRIMs:***
  - The foreign-exchange-balancing requirement has been abolished under the Foreign Investment Law and Decision 46/2003/QÑ-TTg, which states that enterprises do not have to sell foreign exchange to banks to reduce the foreign exchange forced surrender rate to zero percent;
  - Vietnam does not apply import and export balancing requirements;
  - The Foreign Investment Law encourages but does not force companies to buy domestic products per local content requirements. However, in some sectors, taxes and various incentives may be based on how much local content is used in the production of a product; and,
  - Decree 27/2003/ND-CP removed the requirement that a certain level of exports is required to maintain a foreign investment license in some domestic industries, but others remain.
- ***Market Access Commitments*: ** Recently, licensing authorities state that they have been applying the BTA to U.S. investors on a case-by-case basis. In a number of sectors, however, these rights for U.S. investors are not yet clearly provided for in written regulations published in the Official Gazette, as required by the BTA.
- ***Investment Dispute Resolution Commitment*: ** MPI has submitted to the Prime Minister a proposal to accede to the Washington Convention 1965 Resolution on disputes between a state and citizen of another country. MPI is working with other agencies to complete necessary legal

13. Note that this only applies to foreign businesses. Foreign individuals still have to pay a higher price for electricity. Dual prices for other fees had been removed earlier, including for: water, phone installation, air transportation and advertising.

procedures for submitting this Resolution to the President for final approval.

The Common Investment Law and the Uniform Enterprise Law, which are scheduled to be approved in the October 2005 National Assembly session, are expected to meet a number of additional important BTA commitments, including:[14]

- Extension of licensing by registration to all sectors except those with restrictions in the BTA;
- Liberalizing sectors for foreign investment as per international commitments, including those scheduled under the BTA and the WTO accession protocol;
- Removal of restrictions on foreign investment, such as the minimum capital requirement, limits of the establishment of joint stock companies, consensus decision making requirements, and the first refusal right to Vietnamese joint ventures partners; and,
- Full elimination of investment performance requirements in line with the TRIMs Agreement, which is essentially incorporated by reference in the BTA, and for export performance requirements stated in the BTA that go beyond TRIMs.
- Improving investment protection procedures and access to international arbitration facilities.

In addition to commitments regarding investment, Vietnam has made significant progress on implementing other commitments in the BTA that help improve the business environment. These include improving transparency by requiring publication of regulations before their effectiveness, reforming court procedures to make the court more independent and effective, improving the arbitration process, modernizing contract law, reforming legal and banking services, and implementing transactions-based customs procedures.

Although major improvements are being made in the business environment for FDI in Vietnam, important problems remain. The findings from the survey of firms reported in Chapter VII summarize the views of the sampled foreign firms. Also, see the website for the Vietnam Business Forum (www.vietnambusinessforum.org) for detailed perspectives by the business community regarding legal and policy issues affecting the investment climate in Vietnam.

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14. At the time of publication of this report, many key elements of the Draft Uniform Enterprise Law and the Draft Common Investment Law are being hotly debated, leaving open many questions as to how both foreign and domestic investment and company registration will be facilitated and/or regulated.

For Vietnam to compete effectively with other potential investment sites, especially Vietnam's dynamic neighbors in the region, including China and other ASEAN countries, it will be important to raise continually investors' confidence through faithful implementation of its international agreements and steady improvements in the domestic business environment.

C. Expected Impact of the BTA on Overall and U.S. FDI into Vietnam

When analyzing the impact of the BTA on FDI, it is important to take into account the relative competitive advantages of firms in Vietnam, the United States and third countries. The competitive advantage of U.S. companies typically focus on more capital/skill/technology-intensive sectors such as financial, legal, consulting and distribution services, oil and gas and other capital-intensive natural-resource-based production, chemicals and pharmaceuticals, and information technology goods and services. U.S. firms are typically strong in sectors where intellectual property is important. Vietnam's comparative advantage for exports, on the other hand, tends toward labor-intensive sectors such as clothing, furniture and footwear, but also include oil and gas reserves and agricultural and fishery sectors. While U.S. buyers for many sectors have an aggressive presence in Vietnam, it is relatively rare for U.S. firms to invest in labor-intensive export production.[15] For these sectors, FDI from Vietnam's East Asian neighbors is much more typical. As such, this analysis would predict that the opening of the U.S. market for labor-intensive exports from Vietnam would increase FDI primarily from regional Asian investors rather than the United States. Over time, however, Vietnamese exports should diversify into sectors

15. The case of NIKE's role in Vietnam is a good example of this situation. NIKE is one of, if not, the largest purchaser of Vietnamese products, but it actually does not own any factories in Vietnam. All NIKE products are produced on a contract basis. In 2001, NIKE purchased US$450 million exports from Vietnam produced by 6 foreign-invested shoe makers and 20 garment factories. By 2004, NIKE had increased exports from Vietnam to US$728 million purchased from 9 foreign-invested shoe makers and 30 garment factories. These firms in combination employed about 130,000 people in Vietnam. Vietnam is the second largest manufacturing base for NIKE athletic shoes, accounting for 22 percent of NIKE's total global volume. Clearly, NIKE has expanded strongly its purchases of goods from Vietnam since the coming into effect of the BTA. Also clearly, in this case, the BTA has stimulated greater FDI into Vietnam from regional investors such as Taiwan and Korea to produce products for NIKE, and has stimulated domestic investment in factories that enter into contract manufacturing relationships with the NIKE buyers. This information on NIKE is based on an interview between Ms. Amanda Tucker, Country Manager, NIKE Vietnam and Le Duc Tan reported in the *Vietnam Economic Times*, May 18, 2005 and a column from the *Dow Jones Newswire* by Catherine McKinney on the same issue.

where U.S. firms have stronger competitive advantages, and thus it should be expected that export-related U.S. FDI should expand over time.

Firms also will invest in Vietnam because of opportunities to export to countries other than the United States. To the degree that the BTA improves the business environment in Vietnam, such FDI should increase as well. Probably more importantly, however, opportunities in the domestic economy are increasingly attracting FDI. In this regard, the BTA represents one part of a much broader effort by the Vietnamese Government to develop its economy and to improve its business environment. Vietnam's economy has grown at an average of around 7 percent over the last decade, is beginning to industrialize quickly, and has a relatively well-educated population of 82 million with rapidly rising standards of living and steadily declining poverty levels. These strong economic fundamentals, combined with widely perceived political stability, create demand for FDI into Vietnam for building all types of physical and social infrastructure, for building industry to meet the rising consumer and industrial needs of a rapidly growing domestic economy, and for extracting major reserves of natural resources, especially oil and gas. U.S. and non-U.S. investors are being attracted by many of these domestic market opportunities.

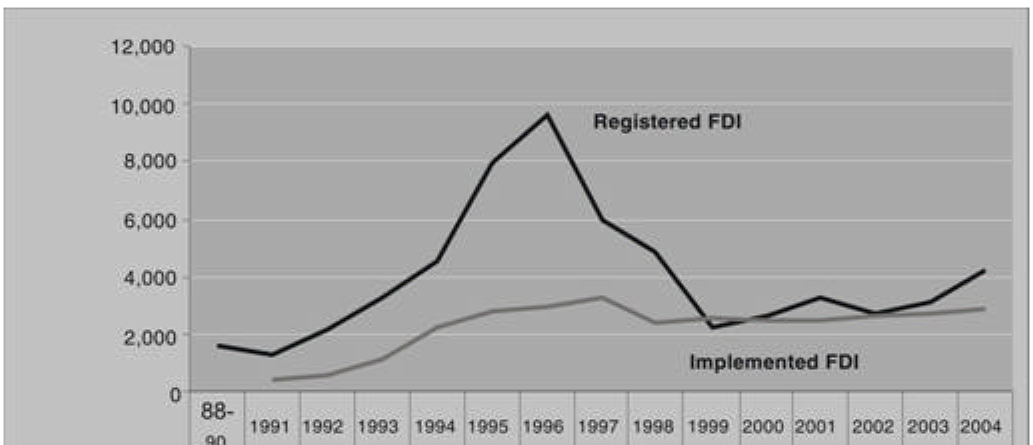
Lastly, effective implementation of the BTA, accession to the WTO and further improvements in the institutional capabilities to implement newly reformed policies more effectively will reduce costs related to doing business in Vietnam and raise the confidence of investors that Vietnam's business environment will continue to get better over time. An important aspect of this is the opening of formerly restricted investment sectors, especially service sectors through the phase-in of BTA requirements and the implementation of the pending WTO accession protocol.

III. OVERALL FDI FLOWS INTO VIETNAM AND THE IMPACT OF THE BTA

As shown in Figure 3, after the spike in the mid-1990s, FDI into Vietnam increased moderately from 1999 to 2004. Although growth in registered FDI picked up from 2001 to 2004 as the BTA was being approved and implemented, most likely representing some increased interest in overall FDI related to the BTA, FDI actually implemented has grown quite modestly since 1997. Furthermore, many other reforms not directly related to the BTA have been enacted from 2001 to 2004, making it difficult to discern the direct impact of the BTA on FDI.

Figure 3: Registered and Implemented FDI From All Countries

(US$ millions)



	88-90	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Registered FDI	1582	1291	2161	3262	4499	7950	9635	5955	4873	2282	2629	3226	2739	3112	4222
Implemented FDI		428	575	1118	2241	2792	2923	3218	2375	2537	2420	2450	2591	2650	2850

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

FDI into Vietnam depends not only on Vietnamese policies, but also on the policies of other countries competing for similar FDI and on the factors affecting foreign investors, both of which are beyond the control of Vietnam.

Table 1 shows that global and regional FDI flows experienced a sharp decline since 2000. Despite the vibrant economies in Southeast Asia and China, FDI inflows into East and Southeast Asia dropped by more than one third from US$142 billion in 2000 to US$97 billion in 2003. The global FDI picture was even bleaker, with a sharp decline by more than one-half, from US$1,388 billion in 2000 to US$560 billion in 2003. Furthermore, FDI to China continued to grow solidly in this period, partly as a result of China's accession to the WTO in 2001, increasing from US$41 billion in 2000 to US$53 billion in 2003.[16] This increase in FDI to China means that FDI to other Southeast and East Asian economies fell even more severely than the regional numbers would imply. If we assess Vietnam's overall FDI performance against this background, Vietnam actually fared well in relative terms compared to most of its regional neighbors. Other than China, Vietnam was one of the few countries in the world where FDI increased from 2000 to 2003. This reflects that Vietnam's reforms appear to have had a more positive impact on FDI than is commonly perceived when country-level results are reviewed in isolation. Nevertheless, Vietnam did not keep up with China's path-breaking success in attracting FDI over this period.

Table 1: FDI Inflows by Region

(US$ billions)

Region/Country	FDI inflows						
	1992-1997 (Annual average)	1998	1999	2000	2001	2002	2003
Developed countries	180.8	472.5	828.4	1,108.0	571.5	489.9	366.6
Western Europe	100.8	263.0	500.0	697.4	368.8	380.2	310.2
European Union	95.8	249.9	479.4	671.4	357.4	374.0	295.2
Other Western Europe	5.0	13.1	20.7	26.0	11.4	6.2	15.1
Japan	1.2	3.2	12.7	8.3	6.2	9.2	6.3
United States	60.3	174.4	283.4	314.0	159.5	62.9	29.8
Developing economies	118.6	194.1	231.9	252.5	219.7	157.6	172.0
Africa	5.9	9.1	11.6	8.7	19.6	11.8	15.0
Latin America and the Caribbean	38.2	82.5	107.4	97.5	88.1	51.4	49.7
Asia and the Pacific	74.5	102.4	112.9	146.2	112.0	94.5	107.3
Asia	74.1	102.2	112.6	146.1	111.9	94.4	107.1
West Asia	2.9	7.1	1.0	1.5	6.1	3.6	4.1
Central Asia	1.6	3.0	2.5	1.9	3.5	4.5	6.1
South, East and South-East Asia	69.6	92.1	109.1	142.7	102.2	86.3	96.9
South Asia	2.5	3.5	3.1	3.1	4.0	4.5	6.1
The Pacific	0.4	0.2	0.3	0.1	0.1	0.1	0.2
Central and Eastern Europe	11.5	24.3	26.5	27.5	26.4	31.2	21.0
World	310.9	690.9	1,086.8	1,388.0	817.6	678.8	559.6

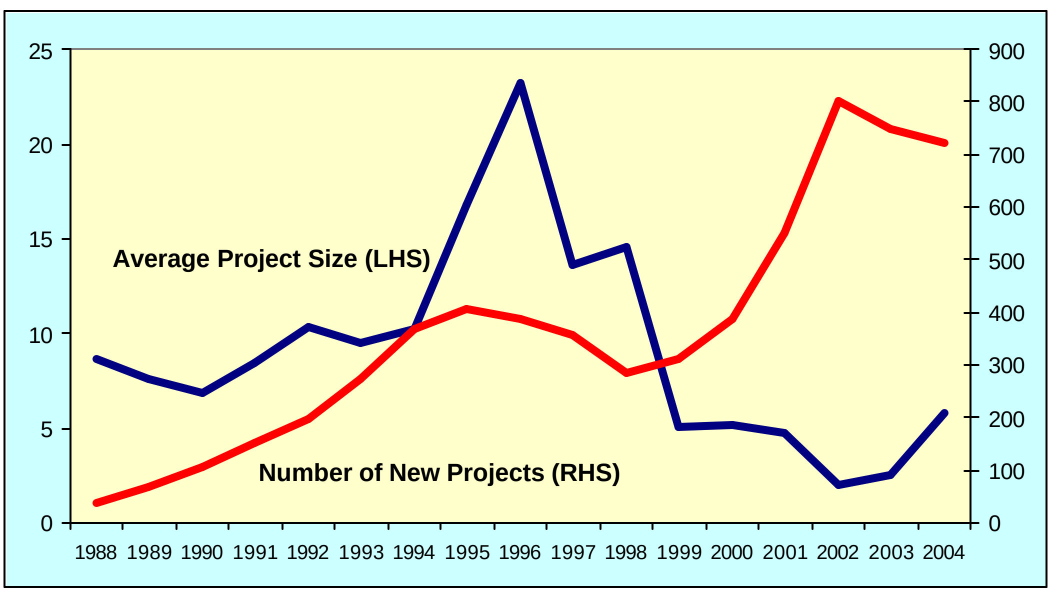
Source: UNCTAD, *World Investment Report, 2004.*

16. See UNCTAD FDI database (www.unctad.org).

An interesting feature of FDI into Vietnam since the mid-1990s peak is that the number of registered FDI projects has increased while the average size of a FDI project has declined (see Figure 4).[17] From around 1996 to 2002, FDI into Vietnam was made increasingly in the form of smaller projects, rather than the larger projects registered in the mid-1990s. This trend reverses after the coming into force of the BTA, with the average size of new registered projects increasing in size somewhat. Nevertheless, from 2002 to 2004, the average FDI project represented a relatively small capital investment, and was made increasingly in light manufacturing industries. This feature is not necessarily good or bad. For such a country with a comparative advantage in labor-intensive exports as Vietnam, one would expect smaller capital investments increasingly in light-manufacturing sectors. On the other hand, this trend reveals that FDI in infrastructure and heavier industry has been relatively small over the last eight years.

Figure 4: The Number and Average Size of New Registered FDI Projects in Vietnam

(US$ millions)



Source: MPI and the General Statistics Office.

In order to explore more directly the implications of the BTA on FDI, we examine FDI flows in clothing, furniture and fisheries, three sectors that have

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17. We use registered new capital to examine new FDI projects because implemented investment in a certain year can represent the culmulative impact of the implementation of a registered investment over time.

experienced strong export growth to the U.S. since the entry into force of the BTA. As shown in Table 2 (also see Figure 1 in the Executive Summary as reference), registered FDI in these three sectors clearly started to pick up in 2000, the year that the BTA was signed, and has continued to post solid results over the last four years. According to staff of the FIA and company interviews, many of these projects were aimed at exporting to the United States. Most of this new FDI was from investors in the East Asian region, with 93 percent of the FDI in the clothing sector from 2000 to 2004 originating from investors in Asia, mostly from Taiwan, Hong Kong, Korea and Singapore. U.S. investors accounted for only 1 percent.[18]

Table 2: Share of FDI in Clothing, Furniture and Fisheries to Overall Registered FDI from 1998 to 2004

(US$ millions)

	1998	1999	2000	2001	2002	2003	2004
Clothing	60	54	122	657	349	337	420
Furniture	52	68	80	108	108	96	232
Fisheries	15	9	16	39	37	52	18
Total registered FDI of three sectors	**127**	**131**	**218**	**804**	**494**	**485**	**670**
Total registered FDI	**4,781**	**2,197**	**2,485**	**3,224**	**2,757**	**3,064**	**4,200**
Share of three sectors in overall registered FDI	**3%**	**6%**	**9%**	**25%**	**18%**	**16%**	**16%**

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

The important contribution of FDI into these three sectors targeted toward export opportunities to the U.S. opened up by the BTA was substantial during this period. As shown in Table 2, the share of the three sectors in total registered capital increased from a mere 3 percent in 1998 to 25 percent in 2001 and then leveled off to around 16 percent in 2003 and 2004. In absolute terms, registered FDI in these sectors increased from US$130 million in 1998 and 1999 to a peak of US$804 million in 2001. FDI in these sectors remained strong from 2002 to 2004, reaching US$670 million in 2004. FDI in these three sectors contributed 17.5 percent of all FDI registered from 2000 to 2004. Clearly, without the major expansion in FDI in these BTA-related sectors, Vietnam's overall FDI performance would have been substantially weaker over the last five years.

FDI in clothing appears to have been affected by the imposition of quotas by the U.S. on Vietnamese clothing exporters in the U.S.-Vietnam Textile Agreement in 2003, as represented by a slight decrease in FDI in 2003. However,

18. These figures are calculated based on data provided by the FIA.

FDI in clothing rebounded quickly in 2004. According to our interviews of garment companies, three reasons were given to explain the strong expansion of FDI in the clothing sector in 2004. First, clothing producers expect to take advantage of the elimination of the U.S. quota when Vietnam accedes to WTO, which they apparently expect to happen in the near future. In this regard, they are investing their funds because they expect that Vietnam will be able to compete effectively with China and other competitors in the global clothing market. Second, some companies have been able to expand the export of quota-free items to the United States. And, third, the elimination of the EU quota on Vietnamese clothing exports opened up new market opportunities. With the positive attitude by foreign investors that Vietnam can compete in an unregulated global market for apparel, reinforced by recent policies to limit imports of apparel products from China into the U.S. and EU, it is expected that FDI in the Vietnamese clothing sector will remain strong, especially if Vietnam accedes to the WTO by the end of 2005 and can benefit from the elimination of U.S. import quotas.

Table 3 shows that implemented FDI in the clothing sector recorded a solid, steady increase from US$84 million in 1998 to US$204 million in 2004. Growth picked up somewhat from 2001 to 2004, the years of BTA implementation. Comparing 1998 to 2004, the share of FDI in clothing to total implemented FDI doubled from 3.5 percent to 7.2 percent. Although this Report focuses on FDI, the opening of the U.S. market and BTA-related improvement in the business and investment environment almost surely has also stimulated domestic investment, including in the clothing sector where a number of Vietnamese firms (often state-owned firms) expanded capacity quickly to meet a surge in demand for exports of clothing to the United States.

Table 3: Implemented FDI in Clothing Compared to Total Implemented FDI from 1998 to 2004

(US$ millions)

	1998	1999	2000	2001	2002	2003	2004
Clothing	84	97	102	141	198	176	204
Total implemented FDI	2,375	2,537	2,420	2,450	2,591	2,650	2,850
Share of clothing in total implemented FDI	3.5%	3.8%	4.2%	5.8%	7.6%	6.6%	7.2%

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

IV. U.S. FDI INTO VIETNAM AND THE IMPACT OF THE BTA

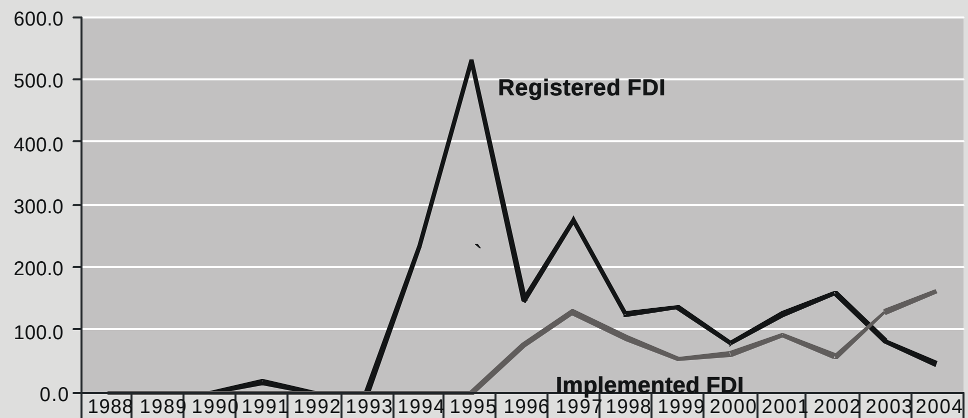
A. Reported U.S. FDI to Vietnam

According to the official statistics normally released by MPI, from 1988 through December 31, 2004, registered U.S. FDI into Vietnam amounted to US$1.3 billion, of which US$730 million had been implemented in 215 projects in manufacturing, oil and gas, agriculture and services sectors (see Table 4). The U.S. ranked 11th among 75 reported investing countries into Vietnam at the end of 2004.

As shown in Figure 5, reported registered U.S. FDI to Vietnam has trended steadily downward since the "boom" period in the mid-1990s. After a bump up in 2001 and 2002 during the period when the BTA was coming into effect, registered U.S. FDI actually fell substantially in 2003 and 2004, even as a number of BTA commitments were set to be phased in. This data would clearly lead to the presumption that the BTA has not had a major effect on U.S. FDI to Vietnam. Implemented U.S. FDI data, however, presents a more positive result, growing solidly in 2003 and 2004. Even with this growth, though, reported implemented U.S. FDI remained much smaller than FDI from many other countries after the BTA (see Figure 5 and Table 9). As shown in Part IV, Section B below, however, a more consistently positive picture is provided regarding U.S. FDI's response to the BTA if FDI from U.S. overseas subsidiaries is taken into account.

Figure 5: Reported Registered and Implemented U.S. FDI from 1988-2004

(US$ millions)



	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Registered FDI	0.3	1.7	0.6	18.9	1.7	0.2	233.7	524.8	144.7	274.0	125.1	135.6	79.6	122.1	159.5	81.3	47.1
Implemented FDI	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	75.1	132.6	89.0	53.4	61.9	92.7	61.3	131.8	162.4

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Tables 4, 5 and 6 provide greater detail with regard to reported U.S. FDI. Most reported U.S. FDI has been in industrial sectors and construction, which have accounted for 71 percent of the total implemented U.S. FDI. The most common type of FDI has been in the form of 100-percent foreign ownership (74 percent of the number of projects), but this has accounted for only 37 percent of total implemented U.S. FDI. Joint ventures and business cooperation contracts (BCCs) accounted for 31 percent and 32 percent of total implemented U.S. FDI, respectively. The high percentage of U.S. FDI in the form of BCCs is due to several large projects in the oil and gas sector, which by regulation can only take the form of BCCs. Most U.S. FDI projects are located in the southern cities/provinces of Ho Chi Minh City, Binh Duong and Dong Nai, in the northern cities/provinces of Hanoi and Hai Duong, and in unspecified oil and gas projects.

Table 4: Reported U.S. FDI by Sector (from 1988 through Dec. 31, 2004)

(US$ millions)

No.	Sector	No. of projects	Initial registered FDI	Implemented FDI	No. of employees
I	***Industry and construction***	***149***	***822***	***519***	***6,281***
1	Heavy industry	80	487	234	2,085
2	Food processing	16	67	9	283
3	Oil and gas	6	124	232	780
4	Construction	11	82	26	214
5	Light industry	36	63	19	2,919
II	***Agriculture - Forestry and Fisheries***	***24***	***153***	***62***	***863***
6	Agriculture and Forestry	22	142	58	760
7	Fisheries	2	12	4	103
III	***Services***	***42***	***316***	***149***	***1,297***
8	Hotel and tourism	5	73	3	0
9	Culture, healthcare, education	11	86	34	1,003
10	Banking and finance	4	65	37	0
11	Transportation, communications and postage	10	44	46	163
12	Apartments and buildings	1	16	8	7
13	Others	10	27	19	124
14	EPZ and IP development	1	5	3	0
	Total	**215**	**1,291**	**730**	**8,441**

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Table 5: Reported U.S. FDI by Form (from 1988 through Dec. 31, 2004)

(US$ millions)

No.	Form of investment	No. of projects	Registered FDI	Implemented FDI	No. of employees
1	100% foreign owned companies	159	853	267	5,811
2	JVs	42	300	229	1,760
3	BCCs	14	139	235	870
	Total	**215**	**1,291**	**730**	**8,441**

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Table 6: Reported U.S. FDI by Province (from 1988 through Dec. 31, 2004)

(US$ millions)

Location	No. of projects	Registered FDI	Implemented FDI	Revenue	No. of employees
Dong Nai	22	249.52	79.94	441.65	835
Ho Chi Minh City	79	233.30	56.91	86.61	1700
Hanoi	22	148.76	76.86	68.99	1096
Binh Duong	32	129.66	61.82	170.04	2757
Oil and Gas	6	123.80	231.80	0.00	780
Hai Duong	2	103.20	147.54	327.37	468
Ba Ria Vung Tau	6	64.43	27.03	91.55	109
Da Nang	2	46.00	0.00	0.00	0
Quang Nam	2	26.28	0.00	0.00	10
Phu Yen	5	26.24	3.32	0.30	109
Ha Tay	3	25.80	21.70	0.00	5
Quang Ninh	2	20.50	2.00	0.00	0
Thua Thien Hue	5	12.53	0.04	0.00	5
Tay Ninh	4	12.50	1.50	0.10	60
Bac Lieu	1	10.46	4.12	2.56	94
Hai Phong	5	10.17	1.60	0.27	133
Quang Tri	2	7.15	1.29	0.00	40
Binh Phuoc	2	6.50	4.50	19.63	86
Can Tho	2	6.45	1.34	3.17	57
Dak Lak	1	4.56	4.56	1.52	30
Yen Bai	2	4.48	0.00	0.00	0
Vinh Phuc	1	4.30	0.00	0.00	0
Lam Dong	1	4.20	1.48	0.00	0
Binh Thuan	1	3.00	0.00	0.00	0
Vinh Long	1	2.39	0.00	0.00	3
Kien Giang	1	2.00	0.00	0.00	0
Long An	1	1.50	0.00	0.00	5
Khanh Hoa	1	1.40	0.30	0.04	9
Thai Binh	1	0.28	0.28	19.93	50
Total	**215**	**1,291**	**730**	**1,234**	**8,441**

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

B. U.S.-Related FDI to Vietnam

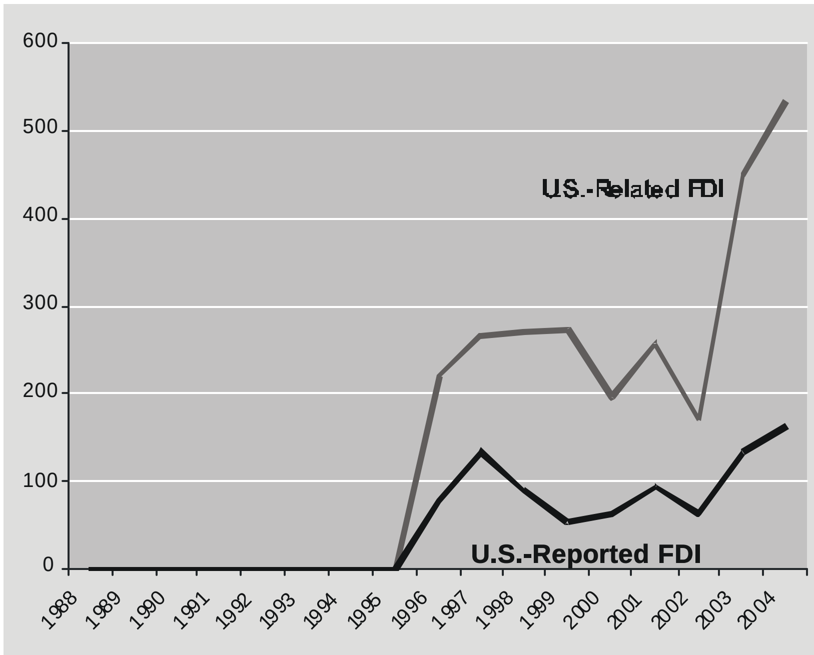
In order to assess the full response of U.S. investors to the BTA, it is necessary to consider not only FDI sourced directly from the U.S., but also to examine FDI made by U.S. overseas subsidiaries. For a number of reasons, we expect that U.S. firms will invest in Vietnam strongly through their overseas subsidiaries, especially their Asian regional headquarters. First, the BTA covers not only investment sourced in the U.S., but it also covers on an equal basis investment made by U.S. subsidiaries resident in third countries. Second, and quite importantly, based on interviews with a number of U.S. firms operating in Vietnam, many noted that U.S. tax laws encourage U.S. firms to source their investment from overseas subsidiaries. Third, there can be managerial and other business operation benefits to having an investment in Vietnam managed by a close-by regional headquarters, especially since most U.S.-related FDI projects in Vietnam tend to be relatively small. A number of prominent U.S. firms operating in Vietnam have sourced their FDI from third countries.[19] For example, American Home, Coca Cola, Procter and Gamble, Caltex and American Standards are invested out of Singapore; Baker & McKenzie and Exxonmobil are sourced from subsidiaries of U.S. operations in Hong Kong; Conoco is invested from the United Kingdom; and Pepsi, British American Tobacco, KPMG and Cisco are investments by U.S. subsidiaries in Holland. A large oil and gas investment by a U.S. firm originated from the Mauritius. As a result, to assess carefully the response of U.S. firms to the impact of the BTA, it is necessary to develop data that reports on FDI from overseas U.S. subsidiaries as well as FDI sourced directly from the United States.

To facilitate this research, based on reports and updates from almost all provinces, the FIA reviewed as many foreign-invested project reports as possible to determine whether the investment was related to a U.S. firm, either a U.S. firm registered directly in the U.S. or a U.S. subsidiary registered in a third country. A new type of FDI data has been calculated – "U.S.-related" FDI. U.S.-related FDI equals FDI reported as sourced from the U.S. (the typical FDI reported by the MPI on a regular basis) plus FDI from U.S. subsidiaries sourced from third countries. Given the limitations of this study, it is not possible to make similar adjustments for FDI from other countries. As a result, this Report cannot re-rank U.S.-related FDI relative to other countries "related" FDI.

19. Many other FDI projects by major U.S. firms, of course, have been sourced directly from the United States. For example, major investments by Ford, Citibank, Kimberly Clark, Cargill, Colgate and Unocal are sourced from the United States. Although considerably more numerous than those sourced from overseas subsidiaries, FDI sourced directly from the U.S. tend to be smaller and are reported by the FIA to have a higher rate of failure than those sourced from third countries.

Figure 6: U.S. Implemented FDI

(US$ millions)



Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects.

Table 7: U.S. Investment by Economic Sector (1988 through Dec. 31, 2004)

(US$ millions)

		U.S.-Related FDI-I				U.S.-Reported FDI-II			
No.	Sector	No. of projects	Initial registered FDI	Imple-mented FDI	No. of employees	No. of project	Initial registered FDI	Imple-mented FDI	No. of employees
I	***Industry and construction***	***176***	***1,751***	***2,208***	***12,637***	***149***	***822***	***519***	***6,281***
1	Heavy industry	92	648	385	3,073	80	487	234	2,085
2	Food processing	19	557	693	2,566	16	67	9	283
3	Oil and gas	8	219	864	1,430	6	124	232	780
4	Construction	15	196	146	1,530	11	82	26	214
5	Light industry	42	131	120	4,038	36	63	19	2,919
II	***Agriculture-Forestry and Fisheries***	***26***	***198***	***87***	***873***	***24***	***153***	***62***	***863***
6	Agriculture and Forestry	24	187	82	770	22	142	58	760
7	Fisheries	2	12	4	103	2	12	4	103
III	***Services***	***65***	***653***	***339***	***3,343***	***42***	***316***	***149***	***1,297***
8	Hotel and tourism	13	267	72	785	5	73	3	0
9	Culture, healthcare, education	12	136	35	1,007	11	86	34	1,003
10	Banking and finance	10	11	103	915	4	65	37	0
11	Transportation, communications and postage	12	67	60	289	10	44	46	163
12	Apartments and buildings	2	*37*	*41*	37	1	*16*	*8*	7
13	Others	15	*33*	*25*	310	10	*27*	*19*	124
14	EPZ and IP development	1	*5*	*3*	0	1	*5*	*3*	0
	Total	***267***	***2,602***	***2,634***	***16,853***	***215***	***1,291***	***730***	***8,441***
		Understatement (I - II)				**52**	***1,310***	***1,904***	**8,412**

Source: MPI. Initial registered capital reported in this table is registered capital at the time of establishment, which does not include subsequent capital changes.[20] Implemented FDI is for active projects, which exclude dissolved and expired projects.

As illustrated in Figure 6 and Table 7, in comparison to the U.S.-based FDI typically reported by MPI, U.S.-related FDI provides a substantially more positive picture with regard to U.S. investor contributions to Vietnam's economy over the last seventeen years and to the response of U.S. investors to the BTA.

20. This is one reason why the U.S.-related implemented capital differs from registered capital.

Looking first at cumulative FDI as is most commonly reported by MPI, U.S.-related registered FDI (which does not include subsequent capital increases) from 1988 through 2004 was US$2.602 billion compared to the reported registered U.S. FDI of US$1.291 billion. The difference is even more profound for implemented FDI, with U.S.-related implemented FDI equaling $2.634 billion compared to the reported U.S. implemented FDI of US$730 million. For the cumulative data, U.S.-related registered FDI is more than double reported registered U.S. FDI, and U.S.-related implemented is more than three and a half times the stock of reported implemented FDI. Interestingly, as shown in Table 8 below, levels of U.S.-related FDI were considerable from 1996 through 2001, before the BTA and during a time when overall FDI to Vietnam was relatively weak. Clearly, these new data on U.S.-related FDI confirm that U.S. firms have been much more strongly invested in the Vietnamese economy over the last ten to fifteen years than the normal reported FDI has led one to believe.

Table 8: U.S.-Related Implemented FDI

(US$ millions)

	U.S.-Related FDI			Reported U.S. FDI			Overall FDI	
Year	**FDI**	**Growth rate**	**Share in overall FDI**	**FDI**	**Growth rate**	**Share in overall FDI**	**FDI**	**Growth rate**
1996	220		8%	75		3%	2923	
1997	266	21%	8%	133	77%	4%	3218	10%
1998	271	2%	11%	89	-33%	4%	2375	-26%
1999	274	1%	11%	53	-40%	2%	2537	7%
2000	196	-28%	8%	62	17%	3%	2420	-5%
2001	258	31%	11%	93	50%	4%	2430	0%
Pre-BTA geometric means		3.2%			4.3%			-3.6%
2002	169	-35%	7%	61	-34%	2%	2591	7%
2003	449	166%	17%	132	116%	5%	2651	2%
2004	531	18%	19%	162	23%	6%	2850	8%
Post-BTA geometric means		27.3%			20.5%			5.5%

Source: MPI. The FDI data in this figure are not adjusted for dissolved and expired projects. This is why cumulative reported FDI in this table exceeds cumulative registered FDI in Table 7.

Figure 6 and Table 8 show that U.S.-related FDI increased significantly after the entry into force of the BTA, especially in the years 2003 and 2004. Over the pre-BTA period, from 1996 to 2001, the average growth of U.S-related implemented FDI was minimal, just around 3 percent per year. From 2001 to 2004, however, U.S.-related implemented FDI surged by an average of 27 percent per year. U.S.-related FDI was particularly strong in 2003 and 2004, achieving levels often 2 times higher than normal years in the past. Furthermore, U.S.-related implemented FDI from 2002 to 2004 totaled to $1.149 billion, while regular reported U.S. FDI came to just US$355 million. In this regard, U.S.-related FDI was around three times higher than the regular reported U.S. FDI since the implementation of the BTA. Furthermore, during this difficult global period for FDI (see Table 1), overall implemented FDI to Vietnam would have increased by just 4 percent from 2000 to 2004 without the robust expansion in U.S.-related FDI of 18 percent growth achieved over this period. Clearly, U.S. investors have responded quite positively to the coming into force of the BTA, and the regular reported FDI data have strongly under-reported how U.S. firms have responded to the BTA.

Lastly, U.S.-related FDI to Vietnam has grown more strongly since the BTA than has non-U.S. FDI (see Figure 7 and Table 9). In 2003, U.S.-related FDI surged to the second largest level among all countries, just below Japan. In 2004, U.S-related FDI exceeded all other countries.[21] This result, in fact, qualifies the argument that the initial investment response to the BTA may be dominated by East Asian firms investing in Vietnam to export labor-intensive products to the newly opened U.S. market. Although it appears that East Asian FDI did increase in some key sectors related to exporting to the U.S. market (as noted above for clothing, furniture and fisheries), U.S.-related FDI also increased markedly as the BTA came into force and was implemented in large part successfully over time.

21. As noted above, it is not possible to re-rank related FDI by country because data are not currently available to calculate "related" FDI for countries other than the United States.

Table 9: Implemented FDI in Vietnam by Country, from 2000 to 2004

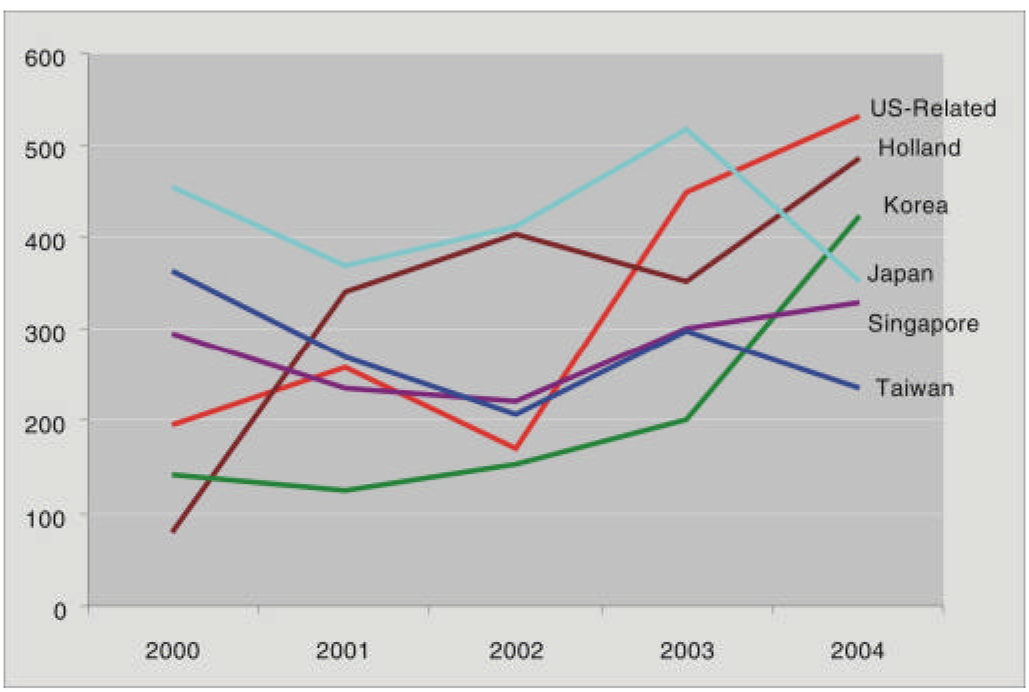
(US$ millions)

No.	Countries	2000	2001	2002	2003	2004
1	U.S.-Related	196	258	169	449	531
2	Holland	79	339	403	350	483
3	Korea	142	125	154	203	421
4	Japan	454	367	411	515	350
5	Singapore	294	235	221	300	328
6	Taiwan	361	269	208	298	235
7	France	76	137	109	169	152
8	Hong Kong	195	87	118	76	145
9	Thailand	35	54	77	67	76
10	Mauritius	45	85	39	94	62
11	China	26	27	49	31	51
12	Russia	216	169	175	74	46
13	Cayman Islands	18	30	40	39	46
14	BVI	123	108	113	46	45
15	Australia	24	14	24	30	41
	Others	265	311	390	226	206

Source: MPI.

Figure 7: Implemented FDI from the Six Biggest Investors in Vietnam

(US$ millions)



Source: MPI. The U.S. trend line is for U.S.-related implemented FDI. Other countries' trend lines are for reported implemented FDI.

Table 10 lists the value of U.S.-related FDI originating from third countries (available only on an accumulated basis from 1988 to 2004). The largest third-country source of U.S.-related FDI is by far Singapore, but Holland, Hong Kong, British Virgin Islands, Bermuda and Mauritius are also important third-country bases for U.S. multinationals to invest into Vietnam. Little U.S.-related FDI was sourced from Japan, Taiwan or Korea.

Table 10: Resident Country for FDI from U.S. Overseas Subsidiaries (1988 through Dec. 31, 2004)

(US$ millions)

No.	Resident country for U.S. overseas subsidiaries with FDI to Vietnam	No. of projects	Registered FDI	Implemented FDI
1	Singapore	13	562	806
2	Holland	4	175	115
3	Hong Kong	8	138	109
4	British Virgin Islands	7	74	23
5	Bermuda	3	69	157
6	Mauritius	1	65	618
7	Swiss	2	60	1
8	Cook Islands	1	50	0
9	Cayman Islands	1	37	41
10	United Kingdom	2	31	15
11	Ukraine	1	16	12
12	Taiwan	4	12	8
13	Bahamas	1	8	1
14	Australia	1	1	0
15	Japan	1	0.5	0.0
16	Thailand	1	0.4	0.7
17	Canada	1	0.3	0.1
	Total	**52**	**1,299**	**1,904**

Source: MPI.

Table 7 breaks down U.S.-related and reported U.S. FDI by economic sector. Cumulated from 1988 through 2004, implemented U.S.-related FDI totaled US$2.634 billion, consisting of 267 projects employing 16,853 people by the end of 2004. In fact, 72 percent of U.S.-related implemented investment worth US$1.9 billion was from overseas subsidiaries of U.S. companies, while only 28 percent has been funded directly from the United States. Table 7 shows that the majority of U.S.-related FDI is in heavy industry, food processing and oil and gas, which have accounted for 74% of accumulated U.S.-related implemented FDI.[22] Most U.S.-related investment is located in Ho Chi Minh City, Binh Duong and Dong Nai in the South, Ha Noi and Hai Duong in the North, and in unspecified locations for oil and gas.

Table 11: U.S. Investment by Form (1988 through Dec. 31, 2004)

(US$ millions)

U.S.-Related FDI-I						U.S.-Reported FDI-II			
No.	Form of investment	No. of projects	Registered FDI	Imple-mented FDI	No. of employees	No. of projects	Registered FDI	Imple-mented FDI	No. of employees
1	100% foreign owned companies	192	1,636	1,104	10,253	159	853	267	5,811
2	JVs	59	732	662	5.080	42	300	229	1,760
3	BCCs	16	234	867	1.520	14	139	235	870
	Total	**267**	**2,602**	**2,634**	**16,853**	**215**	**1,291**	**730**	**8,441**
Understatement (I-II)						**52**	**1,310**	**1,904**	**8,412**

Source: MPI. Registered capital reported in this table is initial registered capital at the time of establishment, which does not include subsequent capital changes. Implemented FDI is for active projects, which excludes dissolved and expired projects.

22. Data are currently not available to provide a more detailed sectoral breakdown of the heavy industry aggregate. Major FDI by Coca-Cola and Pepsi overseas subsidiaries are included in the food processing sector.

Table 12: Distribution of U.S.-Related FDI by Province (1988 through Dec. 31, 2004)

(US$ millions)

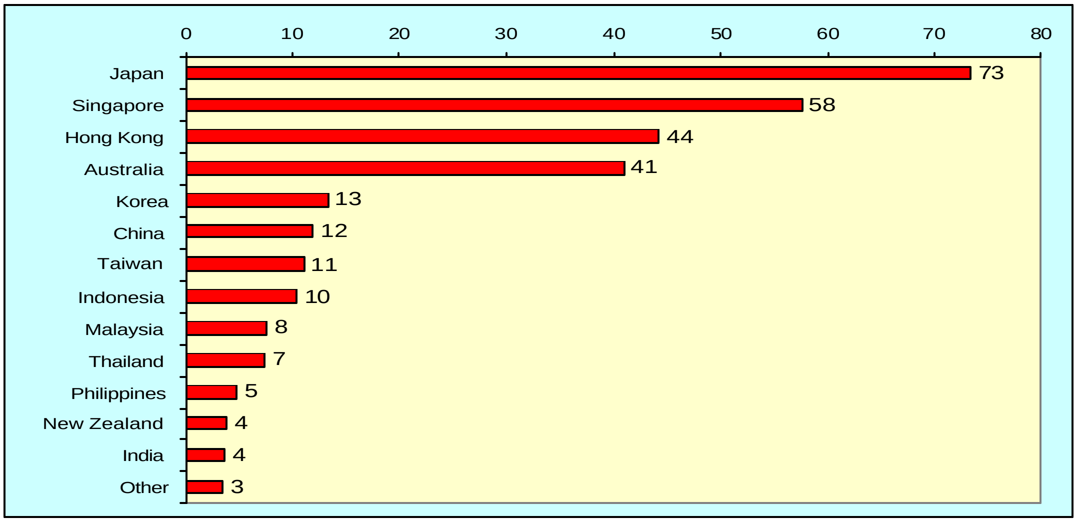
No.	Locations	No. of projects	Registered FDI	Implemented FDI	Revenue	No. of employees
1	Ho Chi Minh City	95	784	820	757	5,015
2	Dong Nai	27	340	153	703	2,241
3	Binh Duong	37	295	222	564	4,079
4	Ha Noi	27	232	118	96	1,355
5	Oil and gas	8	219	864	766	1,430
6	Vung Tau	8	107	72	158	557
7	Hai Duong	2	103	148	327	468
8	Binh Thuan	4	79	15	18	402
9	Hai Phong	11	76	27	55	236
10	Ha Tay	4	75	115	114	93
11	Da Nang	4	64	0.5	0	6
12	Quang Nam	5	61	2	0	27
13	Lam Dong	2	44	53	15	376
14	Phuc Yen	5	26	3	0.3	109
15	Quang Ninh	2	20	2	0	0
16	Tay Ninh	5	13	2	0.1	80
17	Hue	5	13	0.04	0	5
18	Bac Lieu	1	10	4	3	94
19	Quang Tri	2	7	1	0	40
20	Binh Phuoc	2	7	5	20	86
21	Can Tho	2	6	1	3	57
22	Dac Lac	1	5	5	2	30
23	Yen Bai	2	4	0	0	0
24	Vinh Phuc	1	4	0	0	0
25	Vinh Long	1	2	0	0	3
26	Kien Giang	1	2	0	0	0
27	Long An	1	2	0	0	5
28	Khanh Hoa	1	1	0.3	0.04	9
29	Thai Binh	1	0.3	0.3	20	50
	Total	**267**	**2,602**	**2,634**	**3,621**	**16,853**

Source: MPI.

Figure 8 shows U.S. FDI to countries in the Asia-Pacific region. Even with the adjustment to account for U.S.-related FDI to Vietnam, Vietnam would remain a relatively small recipient of FDI compared to U.S. FDI to its neighbors. For example, the U.S.-related FDI of US$2.6 billion is only a third of the U.S. investment stock in Thailand in 2003 and less than 1 percent of the total U.S. investment in the region in 2003. From this perspective, there appears to be ample room for U.S. FDI to Vietnam to grow substantially over the next decade.

Figure 8: U.S. Foreign Investment Stock in Asia - Pacific from 1976 to 2003

(US$ billions)



Source: U.S. Department of Commerce.

V. OUTFLOWS OF FDI FROM VIETNAM AND THE IMPACT OF THE BTA

Vietnamese investors have been making overseas investments since 1989, with a total implemented capital of US$12 million and registered capital of US$225 million (see Tables 13 and 14). After the entry into force of the BTA, some Vietnamese investors have invested in the U.S., such as Kinh Do Confectionery Company. The share of investment in the U.S. relative to total overseas investment by Vietnam, however, is just 1 percent for implemented capital and 3 percent for registered capital.

Investing in the U.S. is one way to enter the U.S. market for Vietnamese companies. From the statistics, it appears that Vietnamese companies are not yet taking advantage of opportunities to invest in the United States.[23] The U.S. is a large market and investment in the U.S. could help to position Vietnamese businesses in that market. This is the experience of many countries. Honda of Japan, for example, has invested in major plants in the U.S. to serve the U.S. market and other countries. Another example that may be useful for Vietnamese businesses is the case of Haier of China, which found investing in the U.S. a good way to reinforce its market position in the U.S. market and to avoid anti-dumping charges.[24] Vietnamese businesses should seriously consider investment opportunities in the U.S. as a way to secure their positions in the U.S. market.

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23. In this regard, although the BTA has greatly increased exposure of the U.S. market for Vietnamese businesses, especially in terms of exports, the BTA did not substantially change the incentives for Vietnamese investors to the United States. This is because the U.S. treated Vietnamese investors essentially just like any other foreign investors into the U.S. before as well as after the BTA came into effect. The U.S. has, for the most part, minimal restrictions on inward foreign direct investment.

24. Minh Le, *"Zhang Ruimin, the Leader of Haier"*, *Saigon Economic Times*, Issue 22-2005 (754), May 25, 2005, Page 54-55.

Table 13: Vietnamese Outward FDI (1989 through December 20, 2004)

(US$ thousands)

No.	Year	No. of projects	Total FDI	Equity	Implemented FDI
1	89-98	18	9,693	9,093	4,800
2	1999	10	12,338	6,773	-
3	2000	15	6,865	6,682	1,210
4	2001	13	7,696	7,696	2,522
5	2002	15	150,916	133,617	1,517
6	2003	25	27,309	26,214	1,956
7	2004	17	11,096	9,283	150
Total		***113***	***225,914***	***199,360***	***12,156***

Source: MPI. This data is only for active projects.

Table 14: Vietnamese Outward FDI by Country (1988 through December 20, 2004)

(US$ thousands)

No.	Host country	No. of projects	Total FDI	Equity	Implemented FDI
1	Iraq	1	100,000	100,000	-
2	Russia	11	34,347	18,171	2,010
3	Laos	33	21,823	15,408	4,288
4	Algeria	1	14,000	14,000	-
5	Cambodia	5	10,125	7,218	989
6	Indonesia	2	9,400	9,400	-
7	Malaysia	2	7,750	7,750	-
8	U.S.	13	6,368	6,088	100
9	Singapore	9	4,387	4,387	1,450
10	Tajikistan	2	3,465	3,465	2,222
11	Germany	3	2,040	2,040	-
12	Japan	4	2,013	1,333	320
13	Ukraine	4	2,857	2,857	-
14	Czech Republic	2	1,069	156	-
15	Kuwaiti	1	1,000	1,000	-
16	Poland	1	900	900	-
17	Uzbekistan	2	850	850	200
18	Brazil	1	800	800	-
19	Australia	2	710	710	378
20	Hong Kong	3	588	373	198
21	Luxemburg	1	350	350	-
22	Thailand	2	305	305	-
23	Taiwan	1	168	1,230	-
24	Bulgaria	1	152	152	-
25	Belgium	1	152	152	-
26	India	1	150	120	-
27	South Korea	1	144	144	-
28	England	2	-	-	-
29	France	1	-	-	-
Total		***113***	***225,914***	***199,360***	***12,156***

Source: MPI. This data is only for active projects.

VI. THE IMPACT OF THE U.S.-VIETNAM BILATERAL TRADE AGREEMENT ON FIRM PERFORMANCE

A. The Sample

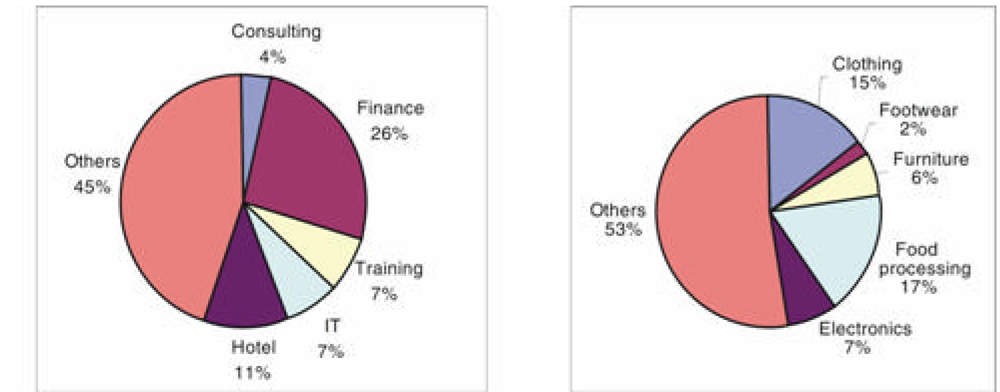
In the first sections of this Report, the impact of the BTA on overall and U.S. FDI has been examined based on quantitative data developed in large part by MPI. In order to have a more thorough understanding of the impact of the BTA, the FIA in cooperation with STAR-Vietnam conducted a firm-level survey of the impact of the BTA on performance of U.S.-invested companies and non-U.S. foreign invested enterprises in Vietnam. The survey aims to improve understanding of the impact of the BTA on the performance of companies in terms of export revenue, investment and employment, as well as to pose various qualitative questions regarding their response to the BTA. The general question posed is whether there has been a difference in firm performance between investors that considered the BTA important for their operations and those that did not. We also look at differences between those firms that exported to the U.S. and those that did not.

Based on the statistics of U.S. companies in Vietnam and the composition of industries and countries of origin of foreign-invested enterprises in Vietnam, the Research Team conducted a mail-out survey of a sample of both U.S. and non-U.S. foreign-invested companies. Questionnaires were sent to 230 U.S.-investors and 280 non-U.S. foreign investors. Non-U.S. foreign investors were selected in such a way as to representative the FDI population in Vietnam. Eighty-one firms responded to the survey – 32 U.S. investors, 47 non-U.S. foreign investors and 2 that did not identify their nationality.[25] Of these 81 responding companies, 30 exported to the U.S. and 43 did not. Goods producing companies accounted for 67 percent of the respondents, with the remaining 33 percent companies operating in service sectors (see Figure 9). It should be noted that although the number of observations is small, especially for some sectors, the Research Team did find relatively consistent answers to key questions, raising confidence that the survey data can support some preliminary conclusions. To supplement the mail out

25. Note that in the reporting tables, the number of responding firms by question differs because some firms did not answer every question in the survey.

survey, seven in-depth interviews were conducted with U.S. and other foreign firms located in Ho Chi Minh City, Binh Duong, Dong Nai and Hanoi.

Figure 9: Composition of Survey Respondents in Services and Goods Production



Source: Survey of foreign firms conducted for this Report.

B. The Impact of the BTA on U.S. and Non-U.S. Foreign Investors in Vietnam

In order to understand the impact of the BTA on investment decisions, the questionnaire includes a question: *"Did you consider the signing/implementing of the BTA in making/expanding investment?"* Out of 69 respondents to this question, 34 (49%) companies reported that they did consider the BTA in making or expanding their investment in Vietnam. Statistical tests also indicate the significant impact of the BTA on the decision of companies in making/expanding their investment in Vietnam.[26] This result indicates the importance of the BTA for foreign investors in Vietnam.

Another question of interest is whether the impact of the BTA would be the same for both U.S. investors and non-U.S. foreign investors. Using a similar statistical test for these two groups, we find that 57 percent of U.S. investors[27] and 43 percent of non-U.S. investors[28] reported that they considered the impact of signing and implementing the BTA on their investment decision. This result of the survey demonstrates that the BTA impacts investment decisions not only by U.S. investors, but also by a substantial number of non-U.S. foreign investors.

26. A statistical test shows that we can reject the null hypothesis that the BTA did not have any impact on investment decisions (t statistic = 8.12).

27. Standard deviation: 9%.

28. Standard deviation: 7%.

The results do show, however, that U.S. investors seem to pay more attention to the BTA than do non-U.S. foreign investors.

Comparing the impact of the BTA on exporters and non-exporters in the survey, no significant difference was found. Forty-nine percent of exporters[29] reported that the BTA is an important factor in their investment decision and 50 percent of non-exporters said the BTA was important.[30]

One question to ask is whether many foreign investors came to invest in Vietnam to export to the U.S. market in response to the coming into effect of the BTA. In order to test this hypothesis, we compare the responses to the above question on the affect of the BTA on investment decisions by FDI exporters and FDI non-exporters. This test indicates that there is no difference between exporters and non-exporters. However, when this test was performed on the basis of whether a particular investor is an exporter to the U.S. market, the test statistic indicates that the BTA has an important impact on the investment/expansion decision of foreign investors who are exporting to the United States.

A related question is whether the BTA has any bearing on the form of investment. Test statistics indicate that the BTA had a more profound impact on the decisions by investors building new factories ("greenfield investment") than for those who bought an existing firm through a merger or acquisition, though the difference is statistically significant only at the 10 percent level. This is understandable because the Foreign Investment Law in Vietnam does not have a provision on investment by merger and acquisition and the Law on Enterprises restricts foreign ownership in domestic joint-stock companies to no more than 30 percent.

C. The Impact of the BTA on Business Performance

To explore the impact of the BTA on the business performance of companies, the Research Team compared several performance indicators between groups of investors. In particular, two pairs of groups were designated:

- Companies that export to the U.S. and companies that do not export to the U.S.; and,
- BTA investors and non-BTA investors.

29. Standard deviation : 8%.
30. Standard deviation: 9%.

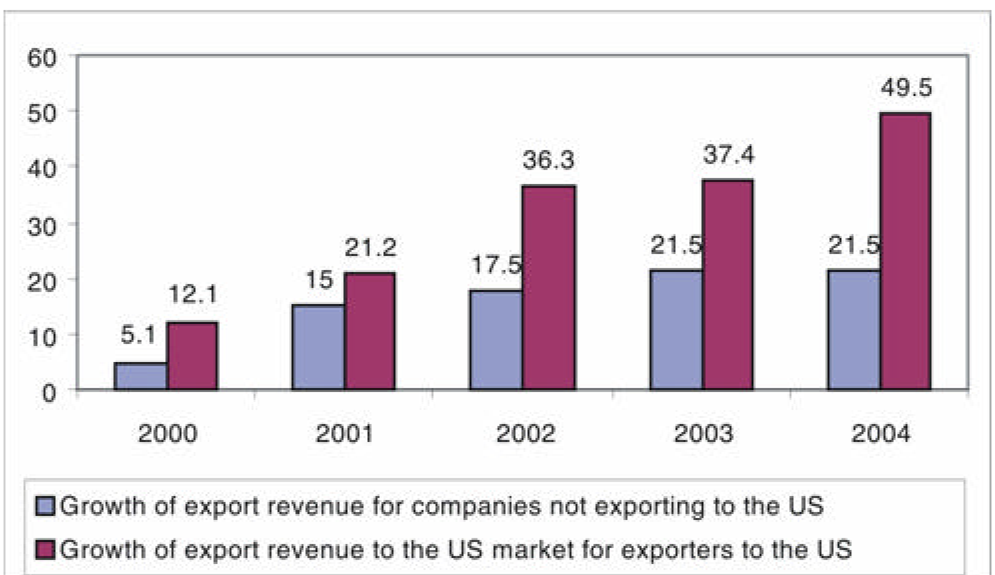
1. Performance of Investors Exporting to the U.S. versus Investors Not Exporting to the U.S.

a. The Impact on Export Revenue Performance

It has been hypothesized that the BTA will attract foreign companies investing in Vietnam as a base for exporting to the U.S. market, building on Vietnam's comparative advantage. To explore this hypothesis, we compare the export revenue for firms exporting to the U.S. market with export revenue for firms not exporting to the U.S. market. As Figure 10 indicates, the growth of revenue from the U.S. market for companies exporting to the U.S. is much higher than the export revenue growth to other markets for companies not exporting to the United States. Before the BTA entered into force, the annual export revenue growth rate of companies exporting to the U.S. in the sample was about 20 percent. After the BTA entered into force, the annual growth rate rose sharply and reached 49.5 percent in 2004.[31] Revenue from non-U.S. markets for companies not exporting to the U.S. did increase after the BTA came into effect, but by far less than for exporters to the United States.

Figure 10: Export Revenue Growth Rates for Foreign Firms Exporting to the U.S. versus Companies Not Exporting to the U.S.

(%)



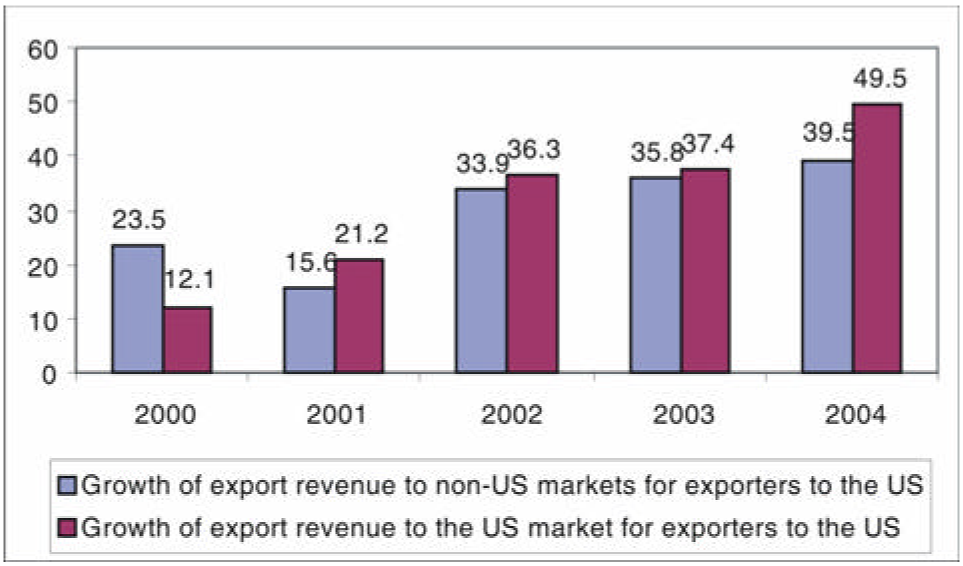
Source: Survey of foreign firms conducted for this Report.

31. This result from the survey was adjusted by dropping firms that reported export growth rates greater than 200 percent to avoid inflating the growth rates. As well, it must be noted that the number of surveyed enterprises exporting to the U.S. is small (20 companies).

For firms exporting to the U.S., annual export revenue growth to the U.S. market and to non-U.S. markets were both higher after the BTA came into effect, but growth to the U.S. market was mildly higher than to non-U.S. markets (see Figure 11). Increased exports to the U.S. market do not seem to have displaced exports to other markets.

Figure 11: Export Growth to the U.S. and Non-U.S. Countries for Firms Exporting to the United States

(%)



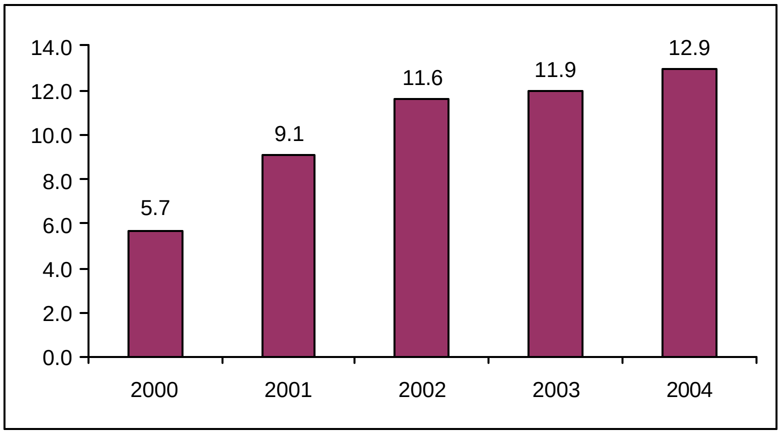
Source: Survey of foreign firms conducted for this Report.

b. The Impact on Implemented FDI

Another indicator of the impact of the BTA is the growth rate of implemented FDI capital. If the BTA has contributed to the creation of a favorable business environment in Vietnam, there should have been significantly stronger growth in implemented capital after the BTA came into effect compared to before the BTA. As shown in Figure 12, the growth rate of implemented FDI capital accelerated from 5.7 percent in 2000 to almost 13 percent in 2004.

Figure 12: Growth Rates of Implemented FDI Capital of Firms in the Survey

(%)

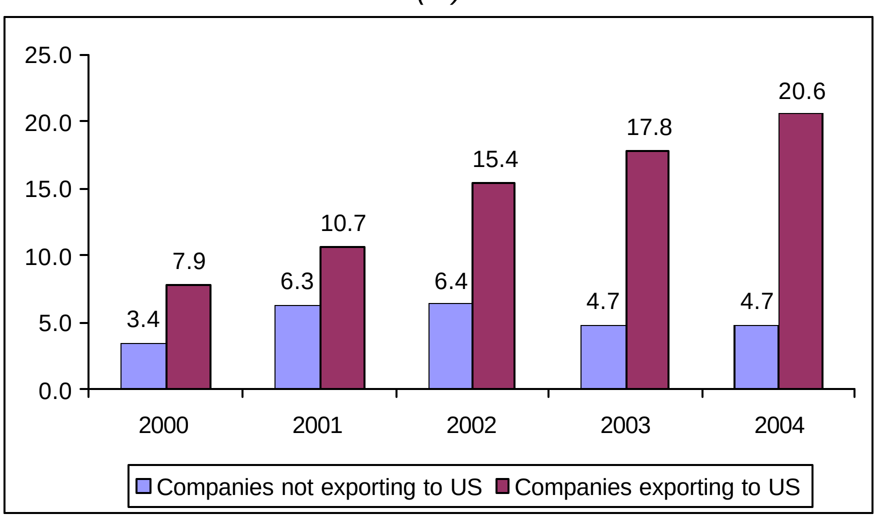


Source: Survey of foreign firms conducted for this Report.

Foreign companies exporting to the U.S. increased FDI significantly faster than did foreign companies not exporting to the United States (see Figure 13). From 2000 through 2004, the growth rate of implemented FDI capital for companies not exporting to the U.S. is only about 5%, while that of companies exporting to the U.S. averages around 15% over the period. Furthermore, the growth rate of FDI by foreign firms exporting to the U.S. accelerated strongly after the BTA, peaking at 20.6 percent in 2004, while the growth in FDI of foreign firms not exporting to the U.S. fell steadily.

Figure 13: Growth Rates of Implemented FDI Capital for Foreign Firms Exporting to the U.S. versus Companies Not Exporting to the U.S.

(%)



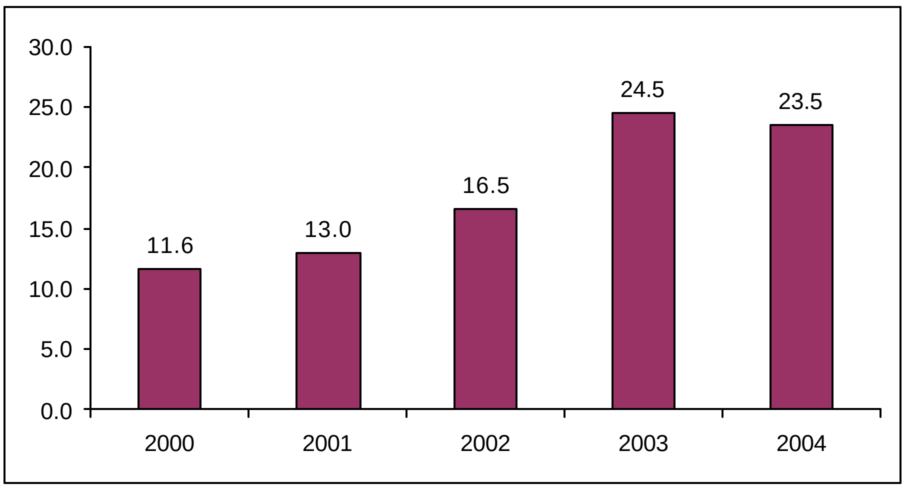
Source: Survey of foreign firms conducted for this Report.

c. The Impact on Employment

An important contribution of FDI projects is the creation of jobs for Vietnamese workers. Figure 14 shows that after the BTA came into effect, employment in the surveyed foreign-invested enterprises grew markedly. Since these growth rates in employment tend to be higher than for implemented FDI, this would imply that FDI over this period has tended to be labor intensive, in line with Vietnam's comparative advantage.

Figure 14: Employment Growth Rates in Surveyed Foreign Firms

(%)

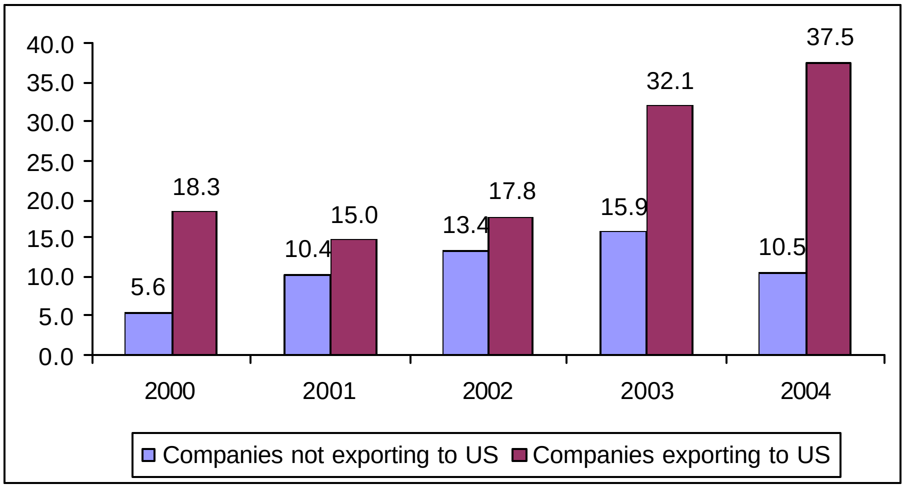


Source: Survey of foreign firms conducted for this Report.

Employment grew much faster for companies exporting to the U.S. than for companies that did not export to the United States (see Figure 15). In line with the trend of increasing export revenue and implemented capital, the employment growth rate in companies exporting to the U.S. market rose from 15 percent in 2001 to 38 percent in 2004. In contrast, companies not exporting to the U.S. experienced little change in their employment after the BTA came into effect.

Figure 15: Employment Growth of Foreign Firms Exporting to the U.S. versus Those Not Exporting to the U.S.

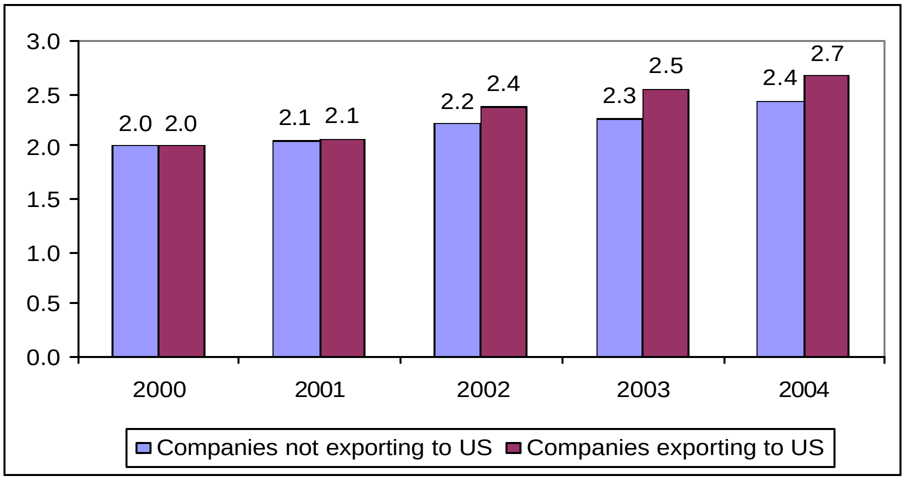
(%)



Source: Survey of foreign firms conducted for this Report.

From the above analysis, we can conclude that companies exporting to the U.S. in the survey substantially increased export revenues, investment and employment after the BTA came into effect. This conclusion is consistent with firms' rating of their business performance presented in Figure 16 below. Before the BTA (2000 and 2001), business performance of both exporters and non-exporters to the U.S. was equivalent. After the BTA, foreign-firms exporting to the U.S. improved their business performance relative to those firms that did not export to the United States.

Figure 16: Business Performance Over Time
(1 is bad, 2 is satisfactory, 3 is good, and 4 is excellent)



Source: Survey of foreign firms conducted for this Report.

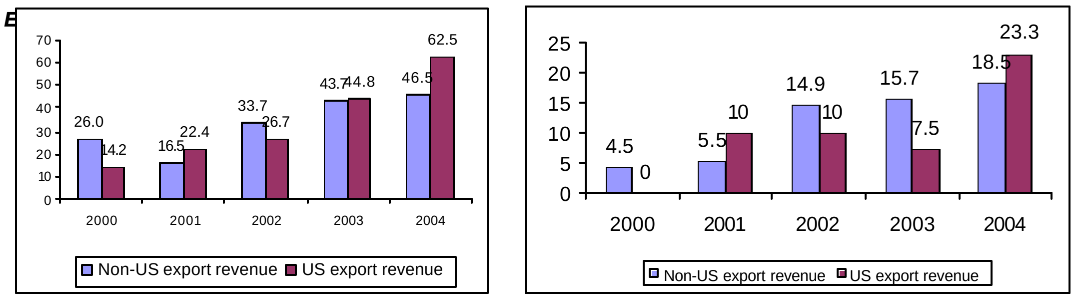
2. Performance of BTA Investors versus Non-BTA Investors

Figure 17 shows the growth of export revenues to the U.S. market and non-U.S. markets for foreign firms who reported that they were affected by the BTA (BTA investors) and those who reported that they were not affected (non-BTA investors). BTA investors increased exports substantially to both U.S. and non-U.S. markets, but by a greater amount to the U.S. market. Similarly, non-BTA investors expanded exports as well to both markets, but by a substantially lower growth rate than did BTA investors. This implies that the companies who say they have been impacted by the BTA have been much more aggressive exporters than non-BTA investors. Both groups of exporters in the survey, however, increased exports substantially to both the U.S. and non-U.S. markets, reflecting an important general "pro-export" impact of BTA implementation on foreign firm operations in Vietnam.

Figure 17: Growth Rate in Export Revenua from the U.S. Market and Non-U.S. Markets

(%)

BTA Investors **Non-BTA Investors**

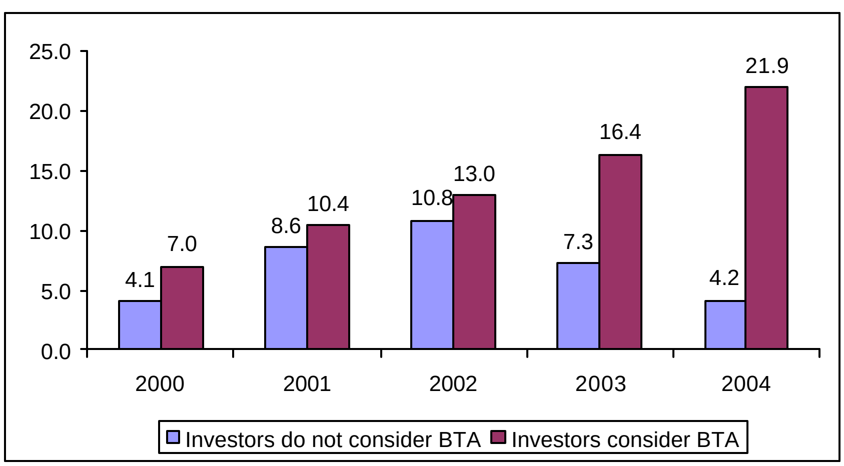


Source: Survey of foreign firms conducted for this Report.

BTA investors expanded FDI capital substantially after the BTA, from 7 percent growth in 2000 to an increase of about 22 percent in 2004 (see Figure 18). The growth rate of implemented FDI for non-BTA investors, on the other hand, declined from 8.6 percent in 2001 to 4.2 percent in 2004.

Figure 18: Growth of Implemented FDI Capital by BTA and Non-BTA Investors

(%)

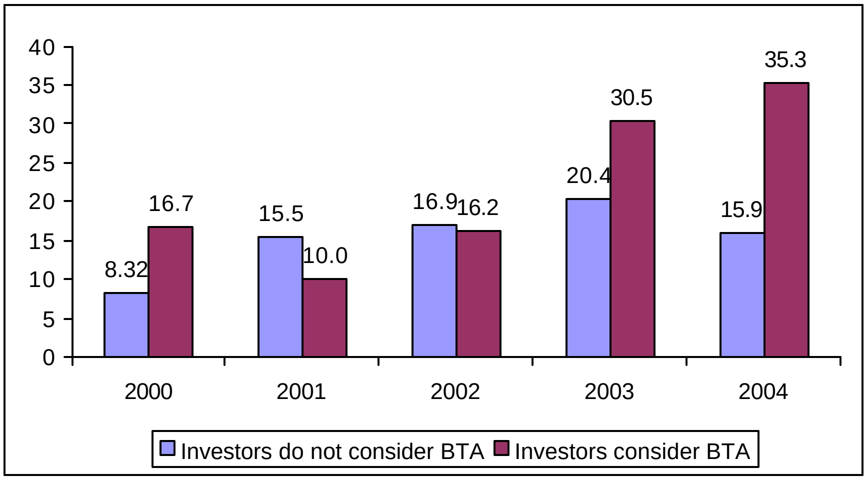


Source: Survey of foreign firms conducted for this Report.

After 2001, the growth in employment of BTA investors rose sharply as compared with that of non-BTA investors (see Figure 19).

Figure 19: Employment Growth of BTA Investors versus Non-BTA Investors

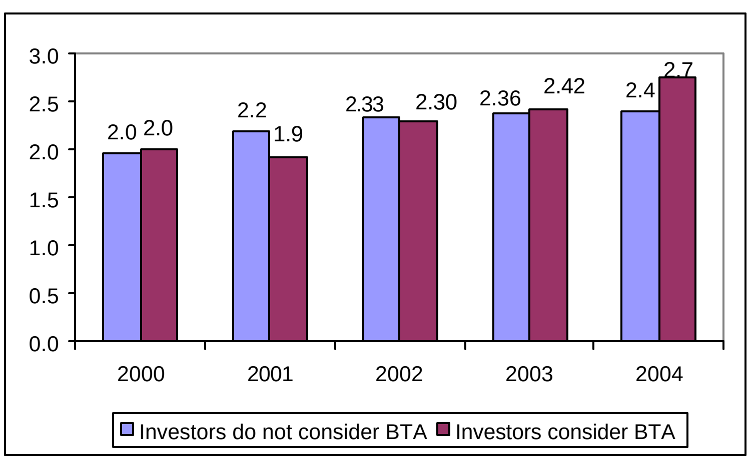
(%)



Source: Survey of foreign firms conducted for this Report.

These three Figures show that BTA investors increased exports, investment and employment considerably more strongly than did non-BTA investors. Consistent with this result, Figure 20 shows that the business performance of BTA investors improved substantially after the BTA came into effect, increasing from 1.9 in 2001 (just below the satisfactory level) to 2.7 in 2004 (almost reaching the good level). Business performance also improved for non-BTA investors after the BTA came into force, but less so than for BTA investors.

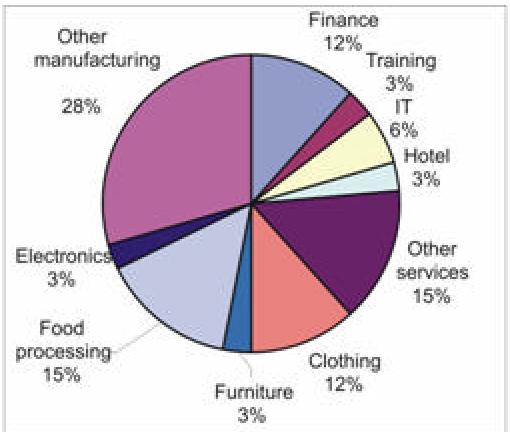
Figure 20: Business Performance Over Time
(1 is bad, 2 is satisfactory, 3 is good, and 4 is excellent)

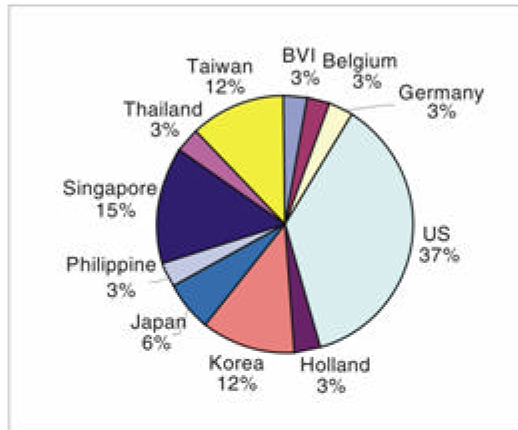


Source: Survey of foreign firms conducted for this Report.

From Figure 21, we can see that a broad range of investors from various sectors and countries considered the BTA in their investment decisions. This is consistent with our previous findings that the BTA is not only important for U.S. but also for foreign investors generally.

Figure 21: Composition of BTA Investors by Sector and Country





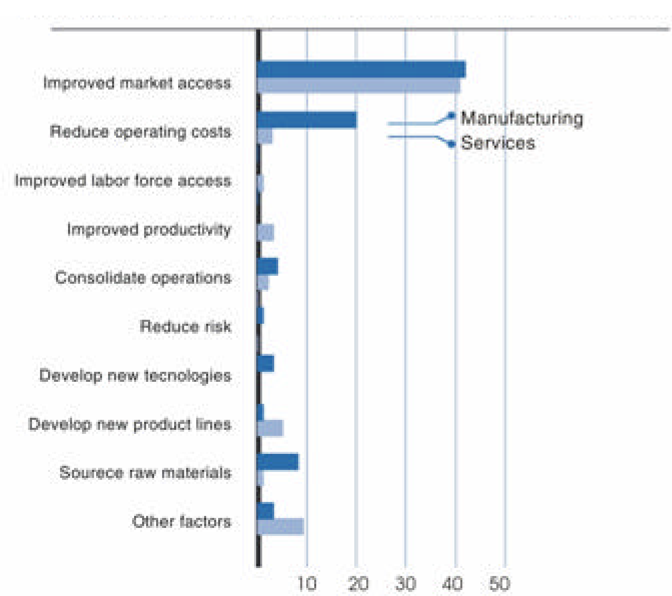
Source: Survey of foreign firms conducted for this Report.

VII. MEASURES TO IMPROVE THE BUSINESS ENVIRONMENT

As discussed in the previous Parts of this Report, the BTA with its comprehensive set of commitments based on international standards should improve the business environment for both foreign and domestic investors. Our analysis in this Part focuses on factors that the surveyed foreign firms feel can improve the investment environment both within and beyond the BTA.

According to the 2004 *World Investment Report* by UNCTAD, FDI has been shifting globally toward service sectors, and investment and trade agreements are having an increasingly important effect on investment decisions.[32] Companies invest abroad for many reasons, but the main ones are market access and cost savings, as presented in Figure 22 from a 2002 MIGA survey of foreign investors.

Figure 22: Most important objective when investing overseas, by sector, in percent



Source: Foreign Direct Investment Survey, January 2002, Multilateral Investment Guarantee Agency, Page 17.

32. *World Investment Report 2004, The Shift Toward Services*, UNCTAD.

Table 15 from the MIGA survey points out that the most important factors in choosing a location for investment are access to customers, social and political stability, the ease of doing business and the reliability of infrastructure and utilities.

Table 15: Top 20 Critical Location Factors, percentage cited as "very influential"

Access to customers	77
Stable social and political environment	64
Ease of doing business	54
Reliability and quality of infrastructure and utilities	50
Ability to hire technical profecssionals	39
Ability to hire management staff	38
Level of corruption	36
Cost fo labor	33
Crime and safety	33
Ability to hire skilled laborers	32
National taxes	29
Cost of utilities	28
Roads	26
Access to raw materials	24
Availability and quality of university and technical training	24
Available and with all services in place	24
Local taxes	24
Access to suppliers	23
Labor relations and unionization	23
Airservice	23

Source: Foreign Direct Investment Survey, January 2002, Multilateral Investment Guarantee Agency, Page 19.

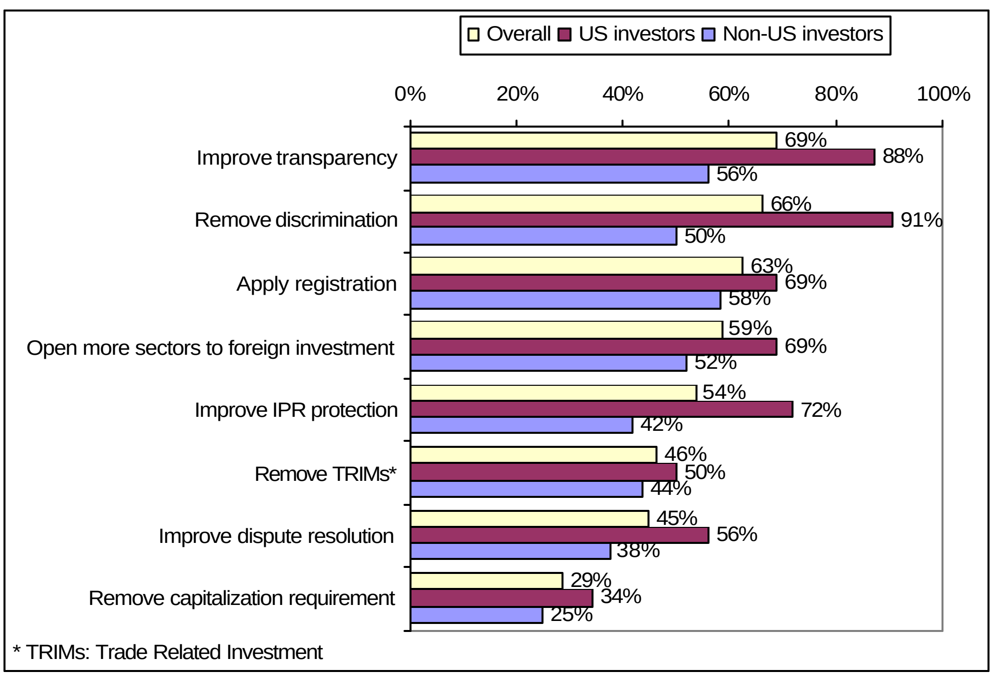
The BTA directly influences many of these concerns specified by international investors, such as:

- *Access to customers:* Opening up of the U.S. market for Vietnamese exports and the opening up of the Vietnamese market for U.S. investors, especially service providers;
- *Ease of doing business and reducing operating costs:*
  - Improving transparency, which reduces opportunities for corruption;
  - Non-discrimination between domestic and foreign investors to facilitate investment and business;
  - Streamlining investment and trading right procedures,
  - Improving commercial dispute settlement procedures;
  - Improving the protection of intellectual property rights;

- o Improving the certainty of the business environment by binding key policies through international agreements; and,
- o Removing the dual pricing system.

In our questionnaire, foreign firms were asked if the implementation of the BTA would help improve their business environment. Figure 23 shows that BTA-related commitments involving transparency and nondiscrimination received the largest number of responses, with 69 and 66 percent of the participating companies, respectively, agreeing that these commitments will help Vietnam to attract more investment. Next in importance are Vietnam's commitments to simplify the licensing regime and to liberalize service sectors, followed by improving IPR protection and removing BTA/WTO-inconsistent investment performance requirements (TRIMs). Although not an important issue for non-U.S. firm, U.S. firms expressed a relatively strong concern for improving dispute settlement procedures. Generally, U.S. investors in the survey responded to these factors in a larger percentage than did non-US foreign investors, which reflects a somewhat higher relative level of interest by U.S. investors in the policies stressed in the BTA.

Figure 23: Commitments in the BTA that Help Improve the Business Environment in Vietnam



Source: Survey of foreign firms conducted for this Report.

It is not a surprise that transparency is considered to influence the investment environment by 69 percent of foreign investors. Companies in our interviews confirmed that the priority concerns for investors in Vietnam are the transparency, consistency and predictability of Vietnam's laws and policies and how they are implemented by Government officials and the courts. This appears particularly true for U.S. investors, possibly because of strict U.S. laws against corruption.

Key commitments on transparency in the BTA require that all measures of general application should be published before coming into effect, and that citizens and companies of the two countries should be allowed to comment on draft laws and regulations of the other country. Vietnam has made significant progress to improve transparency by requiring all legal normative documents issued by the central government to be published in the Official Gazette 15 days before coming into effect. As a result, an average of around 50 Office Gazette Journals are now published each month compared to an average of just 6 in 2001. Recently, normative legal documents issued by local authorities are required to be published (or posted at the Commune level) before entering into force under the Law on the Promulgation of Normative Legal Documents by People's Committees and People's Councils.

More and more legal documents and laws have been made available for public comment by people and businesses, such as the Civil Code, the Commercial Law and the Uniform Enterprise Law. The Vietnam Chamber of Commerce and Industry, supported by STAR, has set up an On-Line Business Forum (www.vibonline.com.vn) that publishes many draft laws and regulations for public comment. However, the process of gathering comments by people and businesses can still be improved to meet the requirements of the BTA.[33] Below are some suggestions to improve transparency and to encourage public comments on drafts:

- Require the publication of all central and local-level legal norms of general application before becoming effective, including those norms of general application currently issued as official letters, dispatches and notices;
- Encourage the process of collecting comments from businesses and the public more generally on all draft legal documents of general application by publishing these drafts on the internet and in the Official Gazette; and,

33. See recent position papers by foreign and domestic investors on this issue at the Vietnam Business Forum at www.vietnambusinessforum.org.

- Announce and publish all relevant administrative rulings of general application and court decisions.

Discrimination is a major obstacle for foreign investment, with 66 percent of participating companies noting the importance of removing discriminatory treatment. As noted in Part II above, Vietnam has now removed the dual pricing system for businesses in all sectors, an encouraging sign for many investors. And, Vietnam is moving toward creating a level playing field between foreign and domestic investors with the development of a new Common Investment Law and a new Unified Enterprise Law.

Fifty-four percent of the firms surveyed (72 percent of the U.S. firms) noted the importance of improving IPR protection to improve the business and investment environment. Stronger IPR protection is needed to attract knowledge-based and "high-tech" investment projects to contribute to the development of a knowledge economy and is a "must" for BTA implementation and WTO accession. Realizing this, Vietnam is developing a new, comprehensive IPR Law that is expected to strengthen considerably the legal framework for IPR protection. In addition, efforts are being made to improve enforcement procedures by strengthening the procedures and capacities of the courts and by improving the coordination and effectiveness of IPR enforcement by administrative agencies. Since IPR protection is a difficult challenge in most countries, especially developing countries, it will take a considerable and sustained effort by the government and right holders to reduce significantly IPR piracy and counterfeiting on the ground.

The survey also asked foreign firms to assess factors affecting FDI that are not necessarily included in the BTA. Table 16 and Figure 24 summarize the answers according to the rank of importance from 1 to 5, with 1 being the most important. Companies in the survey stressed the following as important factors affecting their investment decisions:

1. Ensuring the effective and even enforcement of laws;[34]
2. Joining the WTO;
3. Developing a simple, effective, predictable tax system;
4. Improving infrastructure; and
5. Removing inconsistent regulations.

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34. Effective and even implementation of laws and regulations has a close relationship with commitments under the BTA and WTO, specifically regarding transparency and dispute settlement mechanisms, and the uniform application of laws and regulations.

U.S. and non-U.S. foreign investors differed the most in their views on the importance of tax, trade and investment agreements, with the U.S. firms noting much more strongly the importance of these agreements. On the other hand, U.S. investors emphasized relatively less the importance of infrastructure. More incentives and better access to land were both considered relatively less important by both foreign and U.S. investors.

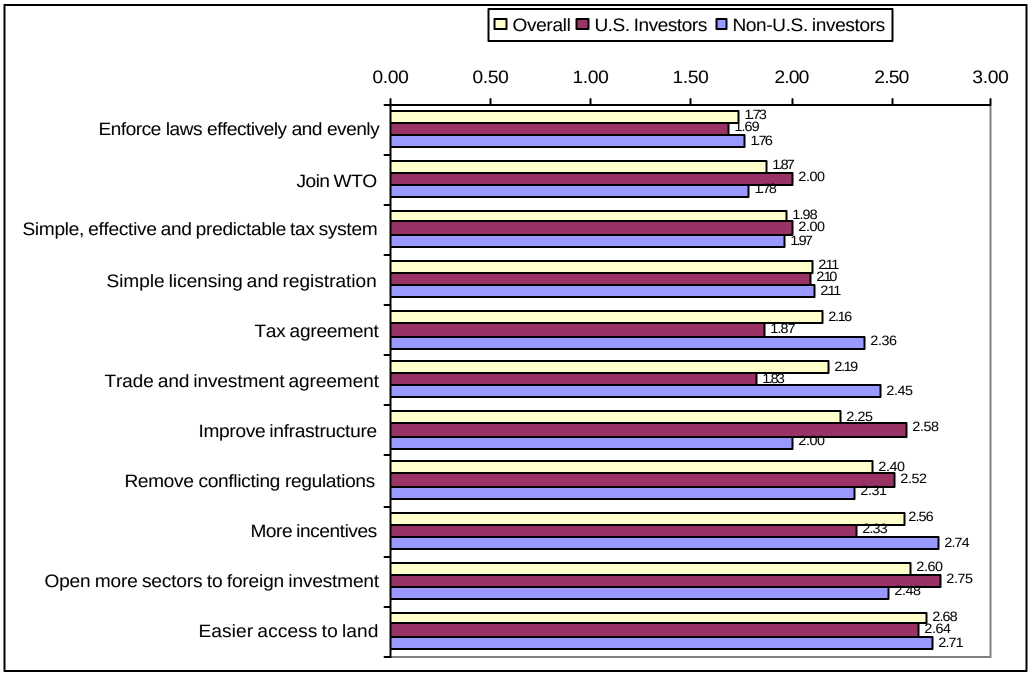
Table 16: Measures to Improve the Investment Environment in Vietnam

	Rank in terms of importance (1 - 5; 1 being the most important)					
Non-U.S. Companies	**1**	**2**	**3**	**4**	**5**	**Score ***
Join WTO	25	4	3	1	4	1.78
Open more sectors to foreign investment	9	9	6	3	4	2.48
Ensure effective and even enforcement of laws	22	10	2	1	3	1.76
Simplify licensing procedures and apply registration to foreign investment	12	13	4	2	1	1.97
Develop a simple, effective, predictable tax system	12	8	6	3	4	2.36
Conclude agreement on avoidance of double taxation	10	7	6	6	2	2.45
Conclude agreement on investment promotion and protection	5	9	9	5	3	2.74
Offer m ore investment incentives	16	6	7	5	1	2.11
Improve infrastructure	15	11	3	3	2	2.00
Remove inconsistent regulations	12	10	7	2	4	2.31
Make it easier to acquire land	8	6	8	5	4	2.71
U.S. Companies						
Join WTO	11	8	4	2	1	2.00
Open more sec tors to foreign investment	6	3	8	5	2	2.75
Ensure effective and even enforcement of laws	19	6	0	2	2	1.69
Simplify licensing procedures and apply registration to foreign investment	13	5	2	1	3	2.00
Develop a simple, effective, predictable tax system	13	4	2	4	0	1.87
Conclude agreement on avoidance of double taxation	11	6	5	1	0	1.83
Conclude agreement on investment promotion and protection	7	8	5	2	2	2.33
Offer more incentives	6	10	2	3		2.10
Improve infrastructure	8	7	3	4	4	2.58
Remove inconsistent regul ations	10	5	5	2	5	2.52
Make it easier to acquire land	5	8	3	2	4	2.64

** The scores reported here are weighted averages of the ratings of firms in the survey.*

Source: Survey of foreign firms conducted for this Report.

Figure 24: Measures to Improve the Investment Environment in Vietnam (ratings are 1 – 5, with 1 being the most important)



Source: Survey of foreign firms conducted for this Report.

VIII. CONCLUSIONS AND SUGGESTIONS FOR FURTHER RESEARCH

Official FDI statistics commonly reported by MPI have long placed U.S. FDI as one of the smaller investors in Vietnam, an anomaly given the size of U.S. investment in many countries throughout the world. This type of data accurately measures the FDI sourced directly from the United States. New FDI data developed by MPI for this Report, however, show that U.S. firms have been more aggressively investing in Vietnam through their overseas subsidiaries for some time, but particularly since the BTA came into effect. U.S.-related implemented FDI, which includes U.S. FDI sourced directly from the U.S. and U.S. FDI sourced from overseas subsidiaries, was around three and a half times greater than the commonly reported U.S. FDI as accumulated over the period from 1988 to 2004. Furthermore, whereas reported registered U.S. FDI actually fell and reported implemented U.S. FDI has grown moderately since the BTA came into effect in late 2001, U.S.-related implemented FDI has grown strongly from 2002 to 2004. While U.S.-related FDI grew by an annual average rate of around 3 percent from 1996 to 2001, growth of U.S.-related FDI accelerated significantly to an average of around 27 percent per year from 2002 to 2004. In fact, in 2003, U.S.-related FDI was higher than any other country's FDI except for Japan, and U.S.-related FDI surpassed every other country's FDI in 2004. Without the strong response of U.S.-related FDI to the BTA, Vietnam's overall FDI would have grown by only 4 percent from 2002 to 2004 rather than increasing as it did by 18 percent.

A survey of foreign firms conducted for this Report showed that the BTA tended to have a positive effect on their investment decisions. This tendency was strongest for U.S. firms and for firms exporting to the United States. Regarding the areas covered by the BTA, firms stressed the importance of improving transparency, removing discrimination between domestic and foreign firms, streamlining the investment licensing system, opening more sectors to FDI and improving IPR enforcement. U.S. firms stressed more than non-U.S. foreign firms the importance of removing discrimination, opening more sectors to FDI, improving IPR protection and improving dispute resolution. When all general considerations for improving the business and investment environment were taken into account, not just those emphasized by the BTA, the firms stressed the importance of enforcing laws evenly and effectively, of joining the WTO and of improving the tax and investment licensing systems. U.S. firms compared to non-U.S. foreign firms stressed the importance of tax, trade and investment agreements. Although firms responding to the survey noted that the investment environment in Vietnam had clearly improved recently, importantly in part as a result of the BTA, they clearly stress the importance of continuing to develop a more transparent legal system with more effective, uniform and predictable enforcement of laws and policies.

This is the first study made on the impact of the BTA on FDI into Vietnam. It has provided new perspectives on how overall and U.S.-related FDI responded to the BTA. The findings of this Report are based on descriptive analysis – no attempt is made to develop a more sophisticated economic model that could more carefully isolate the impact of the BTA relative to other factors affecting FDI into Vietnam. We hope that this Report stimulates new questions and further research on this important issue, and that it can serve as a benchmark for assessing the impact on FDI of Vietnam’s pending WTO accession. To facilitate further research, the Research Team would be happy to provide more details on the data and survey results presented in this Report. And, we encourage MPI and other government agencies to continue to improve the data needed to support meaningful research and analysis.

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